

PITNEY BOWES INC /DE/  
Form 10-Q  
August 01, 2013

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2013

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 1-3579

PITNEY BOWES INC.

(Exact name of registrant as specified in its charter)

Delaware 06-0495050  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

1 Elmcroft Road, Stamford, Connecticut 06926-0700  
(Address of principal executive offices) (Zip Code)

(203) 356-5000  
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

As of July 23, 2013, 201,812,523 shares of common stock, par value \$1 per share, of the registrant were outstanding.

PITNEY BOWES INC.  
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## PART I. FINANCIAL INFORMATION

## Item 1: Financial Statements

## PITNEY BOWES INC.

## CONDENSED CONSOLIDATED STATEMENTS OF INCOME (LOSS)

(Unaudited; in thousands, except per share data)

|  | Three Months Ended June 30, |           | Six Months Ended June 30, |           |
|--|-----------------------------|-----------|---------------------------|-----------|
|  | 2013                        | 2012      | 2013                      | 2012      |
| Revenue:   |                             |           |                           |           |
| Equipment sales  | \$243,644                   | \$224,235 | \$458,643                 | \$444,414 |
| Supplies   | 72,337                      | 70,522    | 146,624                   | 146,887   |
| Software   | 100,482                     | 104,551   | 187,494                   | 208,901   |
| Rentals  | 136,775                     | 145,497   | 273,154                   | 285,886   |
| Financing  | 115,929                     | 122,948   | 232,691                   | 249,696   |
| Support services   | 163,178                     | 171,254   | 328,664                   | 344,772   |
| Business services  | 325,862                     | 327,350   | 649,207                   | 655,447   |
| Total revenue  | 1,158,207                   | 1,166,357 | 2,276,477                 | 2,336,003 |
| Costs and expenses:  |                             |           |                           |           |
| Cost of equipment sales  | 128,426                     | 106,718   | 237,763                   | 203,634   |
| Cost of supplies   | 22,692                      | 20,863    | 45,954                    | 44,734    |
| Cost of software   | 21,435                      | 24,404    | 42,141                    | 45,497    |
| Cost of rentals  | 26,424                      | 31,851    | 54,179                    | 62,076    |
| Financing interest expense   | 19,798                      | 20,642    | 39,673                    | 41,781    |
| Cost of support services   | 104,282                     | 112,123   | 212,291                   | 227,210   |
| Cost of business services  | 248,715                     | 242,010   | 495,611                   | 485,952   |
| Selling, general and administrative                                      | 376,559                     | 380,656   | 748,014                   | 779,852   |
| Research and development   | 31,501                      | 33,811    | 64,836                    | 67,884    |
| Restructuring charges and asset impairments                              | 19,955                      | (585)     | 19,955                    | (585)     |
| Goodwill impairment  | 97,787                      | —         | 97,787                    | —         |
| Other interest expense   | 31,347                      | 30,353    | 62,086                    | 59,720    |
| Interest income  | (1,302)                     | (2,003)   | (3,050)                   | (3,736)   |
| Other expense, net   | —                           | 4,372     | 25,121                    | 1,138     |
| Total costs and expenses   | 1,127,619                   | 1,005,215 | 2,142,361                 | 2,015,157 |
| Income from continuing operations before income taxes                    | 30,588                      | 161,142   | 134,116                   | 320,846   |
| Provision for income taxes   | 15,160                      | 53,113    | 42,899                    | 68,211    |
| Income from continuing operations  | 15,428                      | 108,029   | 91,217                    | 252,635   |
| (Loss) income from discontinued operations, net of tax                   | (20,067)                    | (3,812)   | (23,756)                  | 14,846    |
| Net (loss) income before attribution of noncontrolling interests         | (4,639)                     | 104,217   | 67,461                    | 267,481   |
| Less: Preferred stock dividends attributable to noncontrolling interests | 4,594                       | 4,594     | 9,188                     | 9,188     |
| Net (loss) income - Pitney Bowes Inc.                                    | \$(9,233)                   | \$99,623  | \$58,273                  | \$258,293 |
| Amounts attributable to common stockholders:                             |                             |           |                           |           |
| Net income from continuing operations                                    | \$10,834                    | \$103,435 | \$82,029                  | \$243,447 |
| (Loss) income from discontinued operations, net of tax                   | (20,067)                    | (3,812)   | (23,756)                  | 14,846    |
| Net (loss) income - Pitney Bowes Inc.                                    | \$(9,233)                   | \$99,623  | \$58,273                  | \$258,293 |
| Basic earnings per share attributable to common stockholders:            |                             |           |                           |           |

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|   |          |          |          |         |
|---|----------|----------|----------|---------|
| Continuing operations   | \$0.05   | \$0.52   | \$0.41   | \$1.22  |
| Discontinued operations   | (0.10    | ) (0.02  | ) (0.12  | ) 0.07  |
| Net (loss) income - Pitney Bowes Inc.                           | \$(0.05  | ) \$0.50 | \$0.29   | \$1.29  |
| Diluted earnings per share attributable to common stockholders: |          |          |          |         |
| Continuing operations   | \$0.05   | \$0.51   | \$0.41   | \$1.21  |
| Discontinued operations   | (0.10    | ) (0.02  | ) (0.12  | ) 0.07  |
| Net (loss) income - Pitney Bowes Inc.                           | \$(0.05  | ) \$0.50 | \$0.29   | \$1.29  |
| Dividends declared per share of common stock                    | \$0.1875 | \$0.375  | \$0.5625 | \$0.750 |
| See Notes to Condensed Consolidated Financial Statements        |          |          |          |         |

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PITNEY BOWES INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)  
 (Unaudited; in thousands)

|  | Three Months Ended<br>June 30, |             | Six Months Ended<br>June 30, |           |
|--|--------------------------------|-------------|------------------------------|-----------|
|  | 2013                           | 2012        | 2013                         | 2012      |
| Net (loss) income  | \$(4,639                       | ) \$104,217 | \$67,461                     | \$267,481 |
| Other comprehensive income, net of tax:  |                                |             |                              |           |
| Net unrealized gain on cash flow hedges, net of tax of \$230, \$321, \$574 and \$353, respectively                     | 362                            | 504         | 900                          | 553       |
| Net unrealized (loss) gain on investment securities, net of tax of \$(3,017), \$790, \$(2,842) and \$242, respectively | (4,719                         | ) 1,235     | (4,445                       | ) 378     |
| Amortization of pension and postretirement costs, net of tax of \$4,926, \$7,070, \$11,266 and \$13,967, respectively  | 9,391                          | 10,976      | 20,993                       | 22,964    |
| Foreign currency translations  | (17,554                        | ) (53,267   | ) (59,758                    | ) (19,908 |
| Other comprehensive (loss) income  | (12,520                        | ) (40,552   | ) (42,310                    | ) 3,987   |
| Comprehensive (loss) income  | (17,159                        | ) 63,665    | 25,151                       | 271,468   |
| Less: Preferred stock dividends attributable to noncontrolling interests   | 4,594                          | 4,594       | 9,188                        | 9,188     |
| Total comprehensive (loss) income - Pitney Bowes Inc.  | \$(21,753                      | ) \$59,071  | \$15,963                     | \$262,280 |

See Notes to Condensed Consolidated Financial Statements

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PITNEY BOWES INC.  
CONDENSED CONSOLIDATED BALANCE SHEETS  
(Unaudited; in thousands, except share and per share data)

|  | June 30, 2013 | December 31,<br>2012 |
|--|---------------|----------------------|
| <b>ASSETS</b>  |               |                      |
| Current assets:  |               |                      |
| Cash and cash equivalents  | \$608,568     | \$913,276            |
| Short-term investments   | 22,898        | 36,611               |
| Accounts receivable (net of allowance of \$15,528 and \$20,219, respectively)          | 588,540       | 728,250              |
| Finance receivables (net of allowance of \$26,277 and \$25,484, respectively)          | 1,132,518     | 1,188,292            |
| Inventories  | 141,061       | 179,678              |
| Current income taxes   | 30,578        | 51,836               |
| Other current assets and prepayments   | 158,812       | 114,184              |
| Assets held for sale   | 71,052        | —                    |
| Total current assets   | 2,754,027     | 3,212,127            |
| Property, plant and equipment, net   | 351,606       | 385,377              |
| Rental property and equipment, net   | 230,759       | 241,192              |
| Finance receivables (net of allowance of \$9,824 and \$14,610, respectively)           | 950,656       | 1,026,489            |
| Investment in leveraged leases   | 33,606        | 34,546               |
| Goodwill   | 2,012,752     | 2,136,138            |
| Intangible assets, net   | 143,451       | 166,214              |
| Non-current income taxes   | 93,318        | 94,434               |
| Other assets   | 563,027       | 563,374              |
| Total assets   | \$7,133,202   | \$7,859,891          |
| <b>LIABILITIES, NONCONTROLLING INTERESTS AND STOCKHOLDERS' EQUITY</b>                  |               |                      |
| Current liabilities:   |               |                      |
| Accounts payable and accrued liabilities   | \$1,563,069   | \$1,809,226          |
| Current income taxes   | 208,063       | 240,681              |
| Notes payable and current portion of long-term obligations                             | —             | 375,000              |
| Advance billings   | 448,129       | 452,130              |
| Liabilities related to assets held for sale  | 67,476        | —                    |
| Total current liabilities  | 2,286,737     | 2,877,037            |
| Deferred taxes on income   | 44,460        | 69,222               |
| Tax uncertainties and other income tax liabilities                                     | 144,260       | 145,881              |
| Long-term debt   | 3,654,032     | 3,642,375            |
| Other non-current liabilities  | 685,002       | 718,375              |
| Total liabilities  | 6,814,491     | 7,452,890            |
| Noncontrolling interests (Preferred stockholders' equity in subsidiaries)              | 296,370       | 296,370              |
| Commitments and contingencies (See Note 14)  |               |                      |
| Stockholders' equity:  |               |                      |
| Cumulative preferred stock, \$50 par value, 4% convertible                             | 4             | 4                    |
| Cumulative preference stock, no par value, \$2.12 convertible                          | 613           | 648                  |
| Common stock, \$1 par value (480,000,000 shares authorized; 323,337,912 shares issued) | 323,338       | 323,338              |
| Additional paid-in capital   | 198,938       | 223,847              |
| Retained earnings  | 4,689,969     | 4,744,802            |
| Accumulated other comprehensive loss   | (723,523 )    | (681,213 )           |

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|  |              |              |
|--|--------------|--------------|
| Treasury stock, at cost (121,534,452 and 122,453,865 shares, respectively) | (4,466,998 ) | (4,500,795 ) |
| Total Pitney Bowes Inc. stockholders' equity                               | 22,341       | 110,631      |
| Total liabilities, noncontrolling interests and stockholders' equity       | \$7,133,202  | \$7,859,891  |

See Notes to Condensed Consolidated Financial Statements

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PITNEY BOWES INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (Unaudited; in thousands)

|  | Six Months Ended June 30, |           |
|--|---------------------------|-----------|
|  | 2013                      | 2012      |
| Cash flows from operating activities:  |                           |           |
| Net income before attribution of noncontrolling interests                                  | \$67,461                  | \$267,481 |
| Restructuring payments   | (27,255)                  | (47,875)  |
| Special pension plan contributions   | —                         | (95,000)  |
| Tax payments related to sale of leveraged lease assets                                     | —                         | (84,904)  |
| Adjustments to reconcile net income to net cash provided by operating activities:          |                           |           |
| Goodwill impairment  | 97,787                    | —         |
| Estimated loss on disposal of business   | 31,751                    | —         |
| Gain on sale of leveraged lease assets, net of tax   | —                         | (12,886)  |
| Proceeds from settlement of derivative instruments   | 4,838                     | —         |
| Depreciation and amortization  | 113,702                   | 131,607   |
| Stock-based compensation   | 7,241                     | 8,852     |
| Restructuring charges and asset impairments  | 19,955                    | 1,074     |
| Changes in operating assets and liabilities:   |                           |           |
| (Increase) decrease in accounts receivable   | 67,420                    | 60,176    |
| (Increase) decrease in finance receivables   | 96,928                    | 113,034   |
| (Increase) decrease in inventories   | 29,863                    | (9,428)   |
| (Increase) decrease in other current assets and prepayments                                | (4,810)                   | (13,745)  |
| Increase (decrease) in accounts payable and accrued liabilities                            | (173,479)                 | (100,897) |
| Increase (decrease) in current and non-current income taxes                                | (89,478)                  | 86,555    |
| Increase (decrease) in advance billings  | 6,051                     | 17,178    |
| Increase (decrease) in other operating capital, net  | 31,060                    | 18,610    |
| Net cash provided by operating activities  | 279,035                   | 339,832   |
| Cash flows from investing activities:  |                           |           |
| Short-term and other investments   | 14,633                    | (631)     |
| Capital expenditures   | (73,441)                  | (88,751)  |
| Proceeds from sale of leveraged lease assets   | —                         | 105,506   |
| Net investment in external financing   | (1,021)                   | (3,464)   |
| Reserve account deposits   | (26,189)                  | 2,334     |
| Net cash (used in) provided by investing activities  | (86,018)                  | 14,994    |
| Cash flows from financing activities:  |                           |           |
| Proceeds from the issuance of long-term obligations, net of fees and discounts of \$13,387 | 411,613                   | —         |
| Principal payments of long-term obligations  | (779,637)                 | (550,000) |
| Proceeds from the issuance of common stock under employee stock-based compensation plans   | 3,621                     | 4,274     |
| Dividends paid to stockholders   | (113,106)                 | (150,025) |
| Dividends paid to noncontrolling interests   | (9,188)                   | (9,188)   |
| Net cash used in financing activities  | (486,697)                 | (704,939) |
| Effect of exchange rate changes on cash and cash equivalents                               | (11,028)                  | (6,353)   |
| Decrease in cash and cash equivalents  | (304,708)                 | (356,466) |
| Cash and cash equivalents at beginning of period   | 913,276                   | 856,238   |
| Cash and cash equivalents at end of period   | \$608,568                 | \$499,772 |

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|  |           |          |
|--|-----------|----------|
| Cash interest paid                       | \$95,791  | \$99,477 |
| Cash income tax payments, net of refunds | \$111,318 | \$63,998 |

See Notes to Condensed Consolidated Financial Statements

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PITNEY BOWES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

1. Description of Business and Basis of Presentation

Pitney Bowes Inc. and its subsidiaries (we, us, our or the company) is a global provider of software, hardware and services that enables and integrates both physical and digital communications. We offer a full suite of equipment, supplies, software, services and solutions for managing and integrating physical and digital communication channels. We conduct our business activities in seven reporting segments within two business groups: Small & Medium Business Solutions and Enterprise Business Solutions. See Note 2 for information regarding our reportable segments. The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and the instructions to Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In addition, the December 31, 2012 Condensed Consolidated Balance Sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP. In management's opinion, all adjustments, consisting only of normal recurring adjustments, considered necessary to state fairly our financial position, results of operations and cash flows for the periods presented have been included. Operating results for the periods presented are not necessarily indicative of the results that may be expected for any other interim period or for the year ending December 31, 2013.

In January 2013, the Financial Accounting Standards Board issued Accounting Standards Update No. 2013-01, Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities (ASU 2013-01). ASU 2013-01 requires an entity to disclose gross and net information about transactions that are (1) offset in the financial statements or (2) subject to an enforceable master netting arrangement or similar agreement, regardless of whether the transactions are actually offset in the statement of financial position. The disclosure requirements are effective for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The amounts impacting our disclosure were immaterial at June 30, 2013 and December 31, 2012.

In February 2013, the Financial Accounting Standards Board issued Accounting Standards Update No. 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income (ASU 2013-02). ASU 2013-02 requires an entity to present either parenthetically on the face of the financial statements, or in the notes, significant amounts reclassified from each component of accumulated other comprehensive income and the income statement line items affected by the reclassification. The new standard is effective for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The adoption of this standard resulted in additional disclosures, but did not impact our financial condition, results of operations or cash flows.

During the fourth quarter of 2012, we determined that changes in certain investment-related working capital accounts that were classified as cash flows from operating activities in the Condensed Consolidated Statement of Cash Flows should have been classified as cash flows from investing activities. Accordingly, the Condensed Consolidated Statement of Cash Flows for the period ended June 30, 2012 has been revised to reflect the correct classification of cash flows, resulting in a decrease in cash provided by operating activities and a corresponding increase in cash provided by investing activities of \$30 million.

These statements should be read in conjunction with the financial statements and notes thereto included in our Annual Report to Stockholders on Form 10-K for the year ended December 31, 2012 (the 2012 Annual Report). Certain prior year amounts have been reclassified to conform to the current period presentation.

PITNEY BOWES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

2. Segment Information

We conduct our business activities in seven reporting segments within two business groups, Small & Medium Business Solutions and Enterprise Business Solutions. The principal products and services of each of our reporting segments are as follows:

Small & Medium Business Solutions:

North America Mailing: Includes the U.S. and Canadian revenue and related expenses from the sale, rental and financing of our mail finishing, mail creation, shipping equipment and software; supplies; support and other professional services; and payment solutions.

International Mailing: Includes the revenue and related expenses from the sale, rental and financing of our mail finishing, mail creation, shipping equipment and software; supplies; support and other professional services; and payment solutions outside North America.

Enterprise Business Solutions:

Production Mail: Includes the worldwide revenue and related expenses from the sale, support and other professional services of our high-speed, production mail systems, sorting and production print equipment and related software.

Software: Includes the worldwide revenue and related expenses from the sale and support services of non-equipment-based mailing, client relationship, and communication and location intelligence software.

Management Services: Includes primarily the U.S. and Canadian revenue and related expenses from facilities management services; secure mail services; reprographic, document management services; print outsourcing services; and litigation support and eDiscovery services.

Mail Services: Includes worldwide revenue and related expenses from presort mail services and cross-border ecommerce solutions.

Marketing Services: Includes revenue and related expenses from direct marketing services for targeted clients.

Segment earnings before interest and taxes (EBIT), a non-GAAP measure, is determined by deducting from segment revenue the related costs and expenses attributable to the segment. Segment EBIT excludes interest, taxes, general corporate expenses, restructuring charges and impairment charges, which are not allocated to a particular business segment. Management uses segment EBIT to measure profitability and performance at the segment level.

Management presents segment EBIT because it believes segment EBIT provides investors with an analysis of the company's operating performance and underlying trends of the businesses. Segment EBIT may not be indicative of our overall consolidated performance and therefore, should be read in conjunction with our condensed consolidated results of operations.

Prior period segment information in the tables below have been revised to reflect the International Management Services (PBMSi) business and International Mailing Services (IMS) operations as discontinued operations (see Note 4).

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

Revenue and EBIT by business segment was as follows:

|   | Three Months Ended June 30, |             | Six Months Ended June 30, |             |
|---|-----------------------------|-------------|---------------------------|-------------|
|   | 2013                        | 2012        | 2013                      | 2012        |
| <b>Revenue:</b>                                       |                             |             |                           |             |
| North America Mailing                                 | \$432,889                   | \$453,484   | \$863,264                 | \$914,789   |
| International Mailing                                 | 164,556                     | 165,480     | 332,011                   | 333,494     |
| Small & Medium Business Solutions                     | 597,445                     | 618,964     | 1,195,275                 | 1,248,283   |
| Production Mail                                       | 144,986                     | 123,067     | 263,788                   | 238,083     |
| Software  | 92,242                      | 99,874      | 172,963                   | 200,201     |
| Management Services                                   | 174,708                     | 180,562     | 351,278                   | 360,702     |
| Mail Services   | 119,058                     | 108,045     | 237,913                   | 222,681     |
| Marketing Services                                    | 29,768                      | 35,845      | 55,260                    | 66,053      |
| Enterprise Business Solutions                         | 560,762                     | 547,393     | 1,081,202                 | 1,087,720   |
| Total revenue   | \$1,158,207                 | \$1,166,357 | \$2,276,477               | \$2,336,003 |
|   | Three Months Ended June 30, |             | Six Months Ended June 30, |             |
|   | 2013                        | 2012        | 2013                      | 2012        |
| <b>EBIT:</b>  |                             |             |                           |             |
| North America Mailing                                 | \$166,363                   | \$167,870   | \$320,868                 | \$346,041   |
| International Mailing                                 | 19,285                      | 21,758      | 37,034                    | 41,755      |
| Small & Medium Business Solutions                     | 185,648                     | 189,628     | 357,902                   | 387,796     |
| Production Mail                                       | 13,617                      | 5,594       | 16,672                    | 8,373       |
| Software  | 15,729                      | 8,487       | 20,619                    | 19,179      |
| Management Services                                   | 14,735                      | 14,222      | 29,097                    | 26,210      |
| Mail Services   | 15,484                      | 28,464      | 34,833                    | 62,709      |
| Marketing Services                                    | 4,181                       | 7,503       | 6,167                     | 12,320      |
| Enterprise Business Solutions                         | 63,746                      | 64,270      | 107,388                   | 128,791     |
| Total EBIT  | 249,394                     | 253,898     | 465,290                   | 516,587     |
| <b>Reconciling items:</b>                             |                             |             |                           |             |
| Interest, net <sup>(1)</sup>                          | (49,843                     | ) (48,992   | ) (98,709                 | ) (97,765   |
| Unallocated corporate and other expenses              | (51,221                     | ) (44,349   | ) (114,723                | ) (98,561   |
| Restructuring charges and asset impairments           | (19,955                     | ) 585       | (19,955                   | ) 585       |
| Goodwill impairment                                   | (97,787                     | ) —         | (97,787                   | ) —         |
| Income from continuing operations before income taxes | \$30,588                    | \$161,142   | \$134,116                 | \$320,846   |

(1) Includes financing interest expense, other interest expense and interest income.

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 3. Finance Assets

## Finance Receivables

Finance receivables are comprised of sales-type lease receivables and unsecured revolving loan receivables.

Sales-type lease receivables are generally due in monthly, quarterly or semi-annual installments over periods ranging from three to five years. Loan receivables arise primarily from financing services offered to our customers for postage and related supplies. Loan receivables are generally due each month; however, customers may rollover outstanding balances.

Finance receivables consisted of the following:

|  | June 30, 2013     |               |              |
|--|-------------------|---------------|--------------|
|  | North<br>America  | International | Total        |
| Sales-type lease receivables                   |                   |               |              |
| Gross finance receivables                      | \$ 1,494,818      | \$ 427,386    | \$ 1,922,204 |
| Unguaranteed residual values                   | 132,817           | 20,202        | 153,019      |
| Unearned income                                | (302,533 )        | (97,076 )     | (399,609 )   |
| Allowance for credit losses                    | (15,604 )         | (7,178 )      | (22,782 )    |
| Net investment in sales-type lease receivables | 1,309,498         | 343,334       | 1,652,832    |
| Loan receivables                               |                   |               |              |
| Loan receivables                               | 395,292           | 48,369        | 443,661      |
| Allowance for credit losses                    | (11,559 )         | (1,760 )      | (13,319 )    |
| Net investment in loan receivables             | 383,733           | 46,609        | 430,342      |
| Net investment in finance receivables          | \$ 1,693,231      | \$ 389,943    | \$ 2,083,174 |
|  |                   |               |              |
|  | December 31, 2012 |               |              |
|  | North<br>America  | International | Total        |
| Sales-type lease receivables                   |                   |               |              |
| Gross finance receivables                      | \$ 1,581,711      | \$ 461,510    | \$ 2,043,221 |
| Unguaranteed residual values                   | 148,664           | 21,025        | 169,689      |
| Unearned income                                | (316,030 )        | (104,258 )    | (420,288 )   |
| Allowance for credit losses                    | (16,979 )         | (8,662 )      | (25,641 )    |
| Net investment in sales-type lease receivables | 1,397,366         | 369,615       | 1,766,981    |
| Loan receivables                               |                   |               |              |
| Loan receivables                               | 414,960           | 47,293        | 462,253      |
| Allowance for credit losses                    | (12,322 )         | (2,131 )      | (14,453 )    |
| Net investment in loan receivables             | 402,638           | 45,162        | 447,800      |
| Net investment in finance receivables          | \$ 1,800,004      | \$ 414,777    | \$ 2,214,781 |

## Allowance for Credit Losses and Aging of Receivables

We estimate our finance receivable risks and provide an allowance for credit losses accordingly. We evaluate the adequacy of the allowance for credit losses based on historical loss experience, the nature and volume of our portfolios, adverse situations that may affect a client's ability to pay, prevailing economic conditions and our ability to manage the collateral and make adjustments to the allowance as necessary. This evaluation is inherently subjective and actual results may differ significantly from estimated reserves.

We establish credit approval limits based on the credit quality of the client and the type of equipment financed. Our policy is to discontinue revenue recognition for lease receivables that are more than 120 days past due and for

unsecured loan receivables that are more than 90 days past due. We resume revenue recognition when payments reduce the account balance aging to 60 days or less past due. Finance receivables deemed uncollectible are written off against the allowance after all collection efforts have been exhausted and management

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## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

deems the account to be uncollectible. We believe that our finance receivable credit risk is limited because of our large number of clients, small account balances for most of our clients, and geographic and industry diversification.

Activity in the allowance for credit losses for finance receivables for the six months ended June 30, 2013 and 2012 was as follows:

|                            | Sales-type Lease Receivables |               | Loan Receivables |               | Total    |
|----------------------------|------------------------------|---------------|------------------|---------------|----------|
|                            | North America                | International | North America    | International |          |
| Balance at January 1, 2013 | \$16,979                     | \$8,662       | \$12,322         | \$2,131       | \$40,094 |
| Amounts charged to expense | 3,022                        | 784           | 4,625            | 524           | 8,955    |
| Accounts written off       | (4,397)                      | (2,268)       | (5,388)          | (895)         | (12,948) |
| Balance at June 30, 2013   | \$15,604                     | \$7,178       | \$11,559         | \$1,760       | \$36,101 |

|                            | Sales-type Lease Receivables |               | Loan Receivables |               | Total    |
|----------------------------|------------------------------|---------------|------------------|---------------|----------|
|                            | North America                | International | North America    | International |          |
| Balance at January 1, 2012 | \$28,661                     | \$12,039      | \$20,272         | \$2,458       | \$63,430 |
| Amounts charged to expense | 288                          | 53            | 2,284            | 422           | 3,047    |
| Accounts written off       | (5,068)                      | (3,051)       | (6,026)          | (591)         | (14,736) |
| Balance at June 30, 2012   | \$23,881                     | \$9,041       | \$16,530         | \$2,289       | \$51,741 |

## Aging of Receivables

The aging of gross finance receivables at June 30, 2013 and December 31, 2012 was as follows:

|                            | Sales-type Lease Receivables |               | Loan Receivables |               | Total       |
|----------------------------|------------------------------|---------------|------------------|---------------|-------------|
|                            | North America                | International | North America    | International |             |
| June 30, 2013              |                              |               |                  |               |             |
| < 31 days                  | \$1,421,203                  | \$398,398     | \$377,122        | \$46,341      | \$2,243,064 |
| > 30 days and < 61 days    | 31,153                       | 8,074         | 10,826           | 1,390         | 51,443      |
| > 60 days and < 91 days    | 20,903                       | 5,304         | 3,071            | 295           | 29,573      |
| > 90 days and < 121 days   | 6,159                        | 4,310         | 1,760            | 197           | 12,426      |
| > 120 days                 | 15,400                       | 11,300        | 2,513            | 146           | 29,359      |
| Total                      | \$1,494,818                  | \$427,386     | \$395,292        | \$48,369      | \$2,365,865 |
| Past due amounts > 90 days |                              |               |                  |               |             |
| Still accruing interest    | \$6,159                      | \$4,310       | \$—              | \$—           | \$10,469    |
| Not accruing interest      | 15,400                       | 11,300        | 4,273            | 343           | 31,316      |
| Total                      | \$21,559                     | \$15,610      | \$4,273          | \$343         | \$41,785    |



## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

|                            | December 31, 2012            |               |                  |               |             |
|----------------------------|------------------------------|---------------|------------------|---------------|-------------|
|                            | Sales-type Lease Receivables |               | Loan Receivables |               |             |
|                            | North America                | International | North America    | International | Total       |
| < 31 days                  | \$1,497,797                  | \$435,780     | \$392,108        | \$45,324      | \$2,371,009 |
| > 30 days and < 61 days    | 37,348                       | 9,994         | 12,666           | 1,368         | 61,376      |
| > 60 days and < 91 days    | 24,059                       | 5,198         | 4,577            | 285           | 34,119      |
| > 90 days and < 121 days   | 6,665                        | 3,327         | 2,319            | 179           | 12,490      |
| > 120 days                 | 15,842                       | 7,211         | 3,290            | 137           | 26,480      |
| Total                      | \$1,581,711                  | \$461,510     | \$414,960        | \$47,293      | \$2,505,474 |
| Past due amounts > 90 days |                              |               |                  |               |             |
| Still accruing interest    | \$6,665                      | \$3,327       | \$—              | \$—           | \$9,992     |
| Not accruing interest      | 15,842                       | 7,211         | 5,609            | 316           | 28,978      |
| Total                      | \$22,507                     | \$10,538      | \$5,609          | \$316         | \$38,970    |

## Credit Quality

The extension of credit and management of credit lines to new and existing clients uses a combination of an automated credit score, where available, and a detailed manual review of the client's financial condition and, when applicable, payment history. Once credit is granted, the payment performance of the client is managed through automated collections processes and is supplemented with direct follow up should an account become delinquent. We have robust automated collections and extensive portfolio management processes. The portfolio management processes ensure that our global strategy is executed, collection resources are allocated appropriately and enhanced tools and processes are implemented as needed.

We use a third party to score the majority of the North America portfolio on a quarterly basis using a commercial credit score. We do not use a third party to score our International portfolios because the cost to do so is prohibitive, it is a localized process and there is no single credit score model that covers all countries.

The table below shows the North America portfolio at June 30, 2013 and December 31, 2012 by relative risk class (low, medium, high) based on the relative scores of the accounts within each class. The relative scores are determined based on a number of factors, including the company type, ownership structure, payment history and financial information. A fourth class is shown for accounts that are not scored. Absence of a score is not indicative of the credit quality of the account. The degree of risk, as defined by the third party, refers to the relative risk that an account in the next 12 month period may become delinquent.

• Low risk accounts are companies with very good credit scores and are considered to approximate the top 30% of all commercial borrowers.

• Medium risk accounts are companies with average to good credit scores and are considered to approximate the middle 40% of all commercial borrowers.

• High risk accounts are companies with poor credit scores, are delinquent or are at risk of becoming delinquent and are considered to approximate the bottom 30% of all commercial borrowers.

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

|                              | June 30,<br>2013 | December 31,<br>2012 |
|------------------------------|------------------|----------------------|
| Sales-type lease receivables |                  |                      |
| Low                          | \$1,145,454      | \$1,016,413          |
| Medium                       | 235,243          | 450,432              |
| High                         | 59,112           | 43,658               |
| Not Scored                   | 55,009           | 71,208               |
| Total                        | \$1,494,818      | \$1,581,711          |
| Loan receivables             |                  |                      |
| Low                          | \$287,172        | \$254,567            |
| Medium                       | 90,956           | 136,069              |
| High                         | 12,426           | 14,624               |
| Not Scored                   | 4,738            | 9,700                |
| Total                        | \$395,292        | \$414,960            |

## Troubled Debt

We maintain a program for U.S. clients in our North America loan portfolio who are experiencing financial difficulties, but are able to make reduced payments over an extended period of time. Upon acceptance into the program, the client's credit line is closed and interest accrual is suspended. There is generally no forgiveness of debt or reduction of balances owed. The balance of loans in this program, related loan loss allowance and write-offs are insignificant to the overall portfolio.

## Leveraged Leases

Our investment in leveraged lease assets at June 30, 2013 and December 31, 2012 consisted of the following:

|  | June 30,<br>2013 | December 31,<br>2012 |
|--|------------------|----------------------|
| Rental receivables                               | \$70,585         | \$83,254             |
| Unguaranteed residual values                     | 13,371           | 14,177               |
| Principal and interest on non-recourse loans     | (44,033)         | (55,092)             |
| Unearned income                                  | (6,317)          | (7,793)              |
| Investment in leveraged leases                   | 33,606           | 34,546               |
| Less: deferred taxes related to leveraged leases | (16,754)         | (19,372)             |
| Net investment in leveraged leases               | \$16,852         | \$15,174             |

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 4. Discontinued Operations and Assets Held for Sale

During the quarter, we entered into two separate agreements to sell PBMSi. The assets and liabilities of PBMSi met held-for-sale classification and all historical amounts are presented as discontinued operations for all periods presented in the Condensed Consolidated Statements of Income. We closed on one of the agreements on July 5, 2013 and expect to close on the second agreement by the end of the third quarter. Total proceeds from these sales will not be material.

In connection with the disposal of PBMSi, amounts in the table below for the three and six months ended June 30, 2013 include an impairment charge of \$15 million to write-off the total carrying value of long-lived assets, a goodwill impairment charge of \$2 million to write-off the total carrying value of goodwill and an estimated loss on disposal of \$15 million. The inputs used to determine the fair value of the long-lived assets and goodwill were classified as Level 3 in the fair value hierarchy.

During the fourth quarter of 2012, we made a strategic decision to exit our IMS operations related to the international delivery of mail and catalogs. All historical amounts related to IMS are presented as discontinued operations in the Condensed Consolidated Statements of Income. As of June 30, 2013, we have sold all of our IMS operations. Total proceeds from these sales were not material.

Discontinued operations also include our Capital Services business that was sold in 2006. For the six months ended June 30, 2012, we recognized \$19 million of tax benefits arising from the resolution of tax examinations.

The following table shows selected financial information included in discontinued operations:

|  | Three Months Ended June 30, |           | Six Months Ended June 30, |           |
|--|-----------------------------|-----------|---------------------------|-----------|
|  | 2013                        | 2012      | 2013                      | 2012      |
| Revenue  | \$47,727                    | \$79,460  | \$116,481                 | \$165,470 |
| Pretax loss  | \$(35,948)                  | \$(4,653) | \$(39,367)                | \$(5,667) |
| Net loss   | \$(17,731)                  | \$(3,812) | \$(20,414)                | \$(4,486) |
| Loss on sale of IMS, net of tax                        | (2,336)                     | —         | (3,342)                   | —         |
| Capital Services                                       | —                           | —         | —                         | 19,332    |
| (Loss) income from discontinued operations, net of tax | \$(20,067)                  | \$(3,812) | \$(23,756)                | \$14,846  |

The assets and liabilities held for sale at June 30, 2013 consist of the following:

|   |          |
|---|----------|
| Accounts receivables                        | \$58,382 |
| Inventories                                 | 2,988    |
| Other current assets and prepayments        | 8,606    |
| Total current assets                        | 69,976   |
| Property, plant and equipment, net          | 598      |
| Other assets                                | 478      |
| Assets held for sale                        | \$71,052 |
| Accounts payable and accrued liabilities    | \$52,573 |
| Advance billings                            | 955      |
| Total current liabilities                   | 53,528   |
| Other non current liabilities               | 13,948   |
| Liabilities related to assets held for sale | \$67,476 |

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 5. Fair Value Measurements and Derivative Instruments

We measure certain financial assets and liabilities at fair value on a recurring basis. Fair value is a market-based measure considered from the perspective of a market participant rather than an entity-specific measure. An entity is required to classify certain assets and liabilities measured at fair value based on the following fair value hierarchy that prioritizes the inputs used to measure fair value:

Level 1 – Unadjusted quoted prices in active markets for identical assets and liabilities.

Level 2 – Quoted prices for identical assets and liabilities in markets that are not active, quoted prices for similar assets and liabilities in active markets or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 – Unobservable inputs that are supported by little or no market activity, may be derived from internally developed methodologies based on management's best estimate of fair value and that are significant to the fair value of the asset or liability.

The following tables show, by level within the fair value hierarchy, our financial assets and liabilities that are accounted for at fair value on a recurring basis at June 30, 2013 and December 31, 2012. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement requires judgment and may affect their placement within the fair value hierarchy.

|   | June 30, 2013 |           |         |           |
|---|---------------|-----------|---------|-----------|
|   | Level 1       | Level 2   | Level 3 | Total     |
| Assets:   |               |           |         |           |
| Investment securities   |               |           |         |           |
| Money market funds / commercial paper                                       | \$209,007     | \$34,398  | \$—     | \$243,405 |
| Equity securities   | —             | 25,682    | —       | 25,682    |
| Commingled fixed income securities  | —             | 27,487    | —       | 27,487    |
| Debt securities - U.S. and foreign governments, agencies and municipalities | 112,060       | 22,758    | —       | 134,818   |
| Debt securities - corporate   | —             | 40,849    | —       | 40,849    |
| Mortgage-backed / asset-backed securities                                   | —             | 179,097   | —       | 179,097   |
| Derivatives   |               |           |         |           |
| Interest rate swaps   | —             | 3,230     | —       | 3,230     |
| Foreign exchange contracts  | —             | 6,547     | —       | 6,547     |
| Total assets  | \$321,067     | \$340,048 | \$—     | \$661,115 |
| Liabilities:  |               |           |         |           |
| Derivatives   |               |           |         |           |
| Foreign exchange contracts  | \$—           | \$(3,306) | \$—     | \$(3,306) |
| Total liabilities   | \$—           | \$(3,306) | \$—     | \$(3,306) |

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

|   | December 31, 2012 |           |         | Total       |
|---|-------------------|-----------|---------|-------------|
|   | Level 1           | Level 2   | Level 3 |             |
| Assets:   |                   |           |         |             |
| Investment securities   |                   |           |         |             |
| Money market funds / commercial paper                                       | \$581,648         | \$34,369  | \$—     | \$616,017   |
| Equity securities   | —                 | 25,106    | —       | 25,106      |
| Commingled fixed income securities  | —                 | 29,359    | —       | 29,359      |
| Debt securities - U.S. and foreign governments, agencies and municipalities | 124,221           | 18,908    | —       | 143,129     |
| Debt securities - corporate   | —                 | 43,926    | —       | 43,926      |
| Mortgage-backed / asset-backed securities                                   | —                 | 162,375   | —       | 162,375     |
| Derivatives   |                   |           |         |             |
| Interest rate swaps   | —                 | 10,117    | —       | 10,117      |
| Foreign exchange contracts  | —                 | 2,582     | —       | 2,582       |
| Total assets  | \$705,869         | \$326,742 | \$—     | \$1,032,611 |
| Liabilities:  |                   |           |         |             |
| Derivatives   |                   |           |         |             |
| Foreign exchange contracts  | \$—               | \$(1,174) | \$—     | \$(1,174)   |
| Total liabilities   | \$—               | \$(1,174) | \$—     | \$(1,174)   |
| Investment Securities   |                   |           |         |             |

The valuation of investment securities is based on the market approach using inputs that are observable, or can be corroborated by observable data, in an active marketplace. The following information relates to our classification into the fair value hierarchy:

**Money Market Funds / Commercial Paper:** Money market funds typically invest in government securities, certificates of deposit, commercial paper and other highly liquid, low-risk securities. Money market funds are principally used for overnight deposits and are classified as Level 1 when unadjusted quoted prices in active markets are available and as Level 2 when they are not actively traded on an exchange. Direct investments in commercial paper are not listed on an exchange in an active market and are classified as Level 2.

**Equity Securities:** Equity securities are comprised of mutual funds investing in U.S. and foreign common stock. These mutual funds are classified as Level 2 as they are not separately listed on an exchange.

**Commingled Fixed Income Securities:** Mutual funds that invest in a variety of fixed income securities including securities of the U.S. government and its agencies, corporate debt, mortgage-backed securities and asset-backed securities. The value of the funds is based on the market value of the underlying investments owned by each fund, minus its liabilities, divided by the number of shares outstanding, as reported by the fund manager. These commingled funds are not listed on an exchange in an active market and are classified as Level 2.

**Debt Securities – U.S. and Foreign Governments, Agencies and Municipalities:** Debt securities are classified as Level 1 where active, high volume trades for identical securities exist. Valuation adjustments are not applied to these securities. Debt securities valued using quoted market prices for similar securities or benchmarking model derived prices to quoted market prices and trade data for identical or comparable securities are classified as Level 2.

**Debt Securities – Corporate:** Corporate debt securities are valued using recently executed transactions, market price quotations where observable, or bond spreads. The spread data used are for the same maturity as the security. These securities are classified as Level 2.

**Mortgage-Backed Securities (MBS) / Asset-Backed Securities (ABS):** These securities are valued based on external pricing indices. When external index pricing is not observable, MBS and ABS are valued based on external price/spread data. These securities are classified as Level 2.

Investment securities include investments held by The Pitney Bowes Bank (the Bank), an indirect wholly owned subsidiary whose primary business is to provide financing solutions to clients that rent or lease postage meters. The Bank's key product offering, Purchase Power, is a revolving credit solution, which enables clients to finance their postage costs when they refill their meter. The Bank also provides a

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

deposit solution to those clients that prefer to prepay postage and earn interest on their deposits. When a client refills their postage meter, the funds are withdrawn from the savings account to pay for the postage. The Bank's assets and liabilities consist primarily of cash, finance receivables, short and long-term investments and deposit accounts.

The Bank's investment securities are classified as available-for-sale and recorded at fair value on the Condensed Consolidated Balance Sheets as cash and cash equivalents, short-term investments and other assets depending on the type of investment and maturity. Unrealized holding gains and losses are recorded, net of tax, in accumulated other comprehensive income.

Available-for-sale securities at June 30, 2013 and December 31, 2012 consisted of the following:

|   | June 30, 2013     |                              |                               |                         |
|---|-------------------|------------------------------|-------------------------------|-------------------------|
|   | Amortized<br>cost | Gross<br>unrealized<br>gains | Gross<br>unrealized<br>losses | Estimated<br>fair value |
| Money market funds / commercial paper                                       | \$26,616          | \$—                          | \$(6                          | ) \$26,610              |
| Debt securities - U.S. and foreign governments, agencies and municipalities | 116,570           | 2,045                        | (3,773                        | ) 114,842               |
| Debt securities - corporate   | 39,793            | 1,505                        | (449                          | ) 40,849                |
| Mortgage-backed / asset-backed securities                                   | 179,016           | 2,163                        | (2,082                        | ) 179,097               |
| Total   | \$361,995         | \$5,713                      | \$(6,310                      | ) \$361,398             |
|   | December 31, 2012 |                              |                               |                         |
|   | Amortized<br>cost | Gross<br>unrealized<br>gains | Gross<br>unrealized<br>losses | Estimated<br>fair value |
| Money market funds / commercial paper                                       | \$44,611          | \$53                         | \$—                           | \$44,664                |
| Debt securities - U.S. and foreign governments, agencies and municipalities | 127,807           | 3,972                        | (56                           | ) 131,723               |
| Debt securities - corporate   | 41,095            | 2,851                        | (20                           | ) 43,926                |
| Mortgage-backed / asset-backed securities                                   | 162,180           | 3,340                        | (3,145                        | ) 162,375               |
| Total   | \$375,693         | \$10,216                     | \$(3,221                      | ) \$382,688             |

Scheduled maturities of investment securities at June 30, 2013 were as follows:

|                                | Amortized<br>cost | Estimated<br>fair value |
|--------------------------------|-------------------|-------------------------|
| Within 1 year                  | \$54,032          | \$54,085                |
| After 1 year through 5 years   | 38,948            | 40,028                  |
| After 5 years through 10 years | 83,026            | 81,492                  |
| After 10 years                 | 185,989           | 185,793                 |
| Total                          | \$361,995         | \$361,398               |

We have not experienced any significant write-offs in our investment portfolio. The majority of our MBS are either guaranteed or supported by the U.S. government. We have no investments in inactive markets that would warrant a possible change in our pricing methods or classification within the fair value hierarchy. Further, we have no investments in auction rate securities.

## Derivative Instruments

In the normal course of business, we are exposed to the impact of interest rate changes and foreign currency fluctuations. We limit these risks by following established risk management policies and procedures, including the use of derivatives. We use derivatives to manage the related cost of debt and to limit the effects of foreign exchange rate fluctuations on financial results. We do not use derivatives for trading or speculative purposes. We record our

derivative instruments at fair value, and the accounting for changes in the fair value of the derivatives depends on the intended use of the derivative, the resulting designation, and the effectiveness of the instrument in offsetting the risk exposure it is designed to hedge.

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## PITNEY BOWES INC.

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As required by the fair value measurements guidance, we have incorporated counterparty credit risk and our credit risk into the fair value measurement of our derivative assets and liabilities, respectively. We derive credit risk from observable data related to credit default swaps. We have not seen a material change in the creditworthiness of those banks acting as derivative counterparties.

The valuation of our interest rate swaps is based on the income approach using a model with inputs that are observable or that can be derived from or corroborated by observable market data. The valuation of our foreign exchange derivatives is based on the market approach using observable market inputs, such as forward rates.

The fair value of our derivative instruments at June 30, 2013 and December 31, 2012 was as follows:

| Designation of Derivatives                        | Balance Sheet Location                    | June 30,<br>2013 | December 31,<br>2012 |
|---|---|------------------|----------------------|
| Derivatives designated as hedging instruments     | Other current assets and prepayments:     |                  |                      |
|   | Foreign exchange contracts                | \$455            | \$78                 |
|   | Other assets:                             |                  |                      |
|   | Interest rate swaps                       | 3,230            | 10,117               |
| Derivatives not designated as hedging instruments | Accounts payable and accrued liabilities: |                  |                      |
|   | Foreign exchange contracts                | (238             | ) (320               |
|   | Other current assets and prepayments:     |                  |                      |
|   | Foreign exchange contracts                | 6,092            | 2,504                |
|   | Accounts payable and accrued liabilities: |                  |                      |
|   | Foreign exchange contracts                | (3,068           | ) (854               |
|   | Total derivative assets                   | \$9,777          | \$12,699             |
|   | Total derivative liabilities              | (3,306           | ) (1,174             |
|   | Total net derivative assets               | \$6,471          | \$11,525             |

## Interest Rate Swaps

Derivatives designated as fair value hedges include interest rate swaps related to fixed rate debt. Changes in the fair value of both the derivative and item being hedged are recognized in earnings. The following represents the results of fair value hedging relationships for the three and six months ended June 30, 2013 and 2012:

| Derivative Instrument | Location of Gain (Loss) | Three Months Ended June 30,               |         |   |             |
|-----------------------|-------------------------|---|---------|---|-------------|
|                       |                         | Derivative Gain<br>Recognized in Earnings |         | Hedged Item Expense<br>Recognized in Earnings |             |
|                       |                         | 2013                                      | 2012    | 2013  | 2012        |
| Interest rate swaps   | Interest expense        | \$774                                     | \$3,446 | \$(2,742                                      | ) \$(10,059 |

| Derivative Instrument | Location of Gain (Loss) | Six Months Ended June 30,                 |         |   |             |
|-----------------------|-------------------------|---|---------|---|-------------|
|                       |                         | Derivative Gain<br>Recognized in Earnings |         | Hedged Item Expense<br>Recognized in Earnings |             |
|                       |                         | 2013                                      | 2012    | 2013  | 2012        |
| Interest rate swaps   | Interest expense        | \$2,768                                   | \$6,773 | \$(8,227                                      | ) \$(20,168 |

## Foreign Exchange Contracts

We enter into foreign currency exchange contracts to mitigate the currency risk associated with the anticipated purchase of inventory between affiliates and from third parties. These contracts are designated as cash flow hedges. The effective portion of the gain or loss on cash flow hedges is included in AOCI in the period that the change in fair value occurs and is reclassified to earnings in the period that the hedged item is recorded in earnings. At June 30, 2013 and December 31, 2012, we had outstanding contracts associated with these

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

anticipated transactions with a notional amount of \$30 million and \$25 million, respectively. The value of these contracts at June 30, 2013 and December 31, 2012 was less than \$1 million.

The amounts included in AOCI at June 30, 2013 will be recognized in earnings within the next 12 months. No amount of ineffectiveness was recorded in earnings for these designated cash flow hedges.

The following represents the results of cash flow hedging relationships for the three and six months ended June 30, 2013 and 2012:

| Derivative Instrument      | Three Months Ended June 30,   |         | Location of Gain (Loss)<br>(Effective Portion) | Gain (Loss) Reclassified<br>from AOCI to Earnings<br>(Effective Portion) |         |
|----------------------------|---|---------|--|--|---------|
|                            | Derivative Gain (Loss)<br>Recognized in AOCI<br>(Effective Portion) |         |  | 2013   | 2012    |
|                            | 2013  | 2012    |  |  |         |
| Foreign exchange contracts | \$170   | \$(150) | ) Revenue                                      | \$(371   | ) \$473 |
|                            |   |         | Cost of sales                                  | 286  | (7      |
|                            |   |         |  | \$(85  | ) \$466 |

| Derivative Instrument      | Six Months Ended June 30,   |         | Location of Gain (Loss)<br>(Effective Portion) | Gain (Loss) Reclassified<br>from AOCI to Earnings<br>(Effective Portion) |         |
|----------------------------|---|---------|--|--|---------|
|                            | Derivative Gain (Loss)<br>Recognized in AOCI<br>(Effective Portion) |         |  | 2013   | 2012    |
|                            | 2013  | 2012    |  |  |         |
| Foreign exchange contracts | \$800   | \$(809) | ) Revenue                                      | \$(753   | ) \$774 |
|                            |   |         | Cost of sales                                  | 412  | (73     |
|                            |   |         |  | \$(341   | ) \$701 |

We also enter into foreign exchange contracts to minimize the impact of exchange rate fluctuations on short-term intercompany loans and related interest that are denominated in a foreign currency. The revaluation of the intercompany loans and interest and the mark-to-market adjustment on the derivatives are both recorded in earnings. Outstanding foreign exchange contracts to buy or sell various currencies had a net asset value of \$3 million at June 30, 2013 and \$2 million at December 31, 2012. All outstanding contracts at June 30, 2013 mature by the end of the year. The following represents the results of our non-designated derivative instruments for the three and six months ended June 30, 2013 and 2012:

| Derivatives Instrument     | Location of Derivative Gain (Loss)          | Three Months Ended June 30, |           |
|----------------------------|---|-----------------------------|-----------|
|                            |   | 2013                        | 2012      |
| Foreign exchange contracts | Selling, general and administrative expense | \$(1,644                    | ) \$1,157 |

| Derivatives Instrument     | Location of Derivative Gain (Loss)          | Six Months Ended June 30, |            |
|----------------------------|---|---------------------------|------------|
|                            |   | 2013                      | 2012       |
| Foreign exchange contracts | Selling, general and administrative expense | \$(5,995                  | ) \$(3,067 |

## Credit-Risk-Related Contingent Features

Certain derivative instruments contain credit-risk-related contingent features that would require us to post collateral based on a combination of our long-term senior unsecured debt ratings and the net fair value of our derivatives. At June 30, 2013, we were not required to post any collateral. The maximum amount of collateral that we would have been required to post at June 30, 2013, had the credit-risk-related contingent features been triggered, was less than \$1 million.

#### Fair Value of Financial Instruments

Our financial instruments include cash and cash equivalents, investment securities, accounts receivable, loan receivables, derivative instruments, accounts payable and debt. The carrying value for cash and cash equivalents, accounts receivable, loans receivable, and accounts payable approximate fair value because of the short maturity of these instruments.

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

The fair value of our debt is estimated based on recently executed transactions and market price quotations. We classify our debt as Level 2 in the fair value hierarchy. The carrying value and estimated fair value of our debt at June 30, 2013 and December 31, 2012 was as follows:

|                | June 30, 2013 | December 31,<br>2012 |
|----------------|---------------|----------------------|
| Carrying value | \$3,654,032   | \$4,017,375          |
| Fair value     | \$3,826,593   | \$4,200,970          |

## 6. Restructuring Charges and Asset Impairments

In order to enhance our responsiveness to changing market conditions, further streamline our business operations, reduce our cost structure and create long-term flexibility to invest in growth, we have identified certain actions that we believe will provide both process and operational improvements. We anticipate that these actions will result in restructuring charges in the range of \$75 to \$125 million and will be recognized as specific initiatives are approved and implemented.

During the quarter, we began implementing certain actions, consisting primarily of workforce reductions, and recorded restructuring charges of \$23 million in connection with the above actions. Restructuring charges for the period also include the reversal of \$3 million for changes in reserves under prior restructuring programs.

Activity in our restructuring reserves for the six months ended June 30, 2013 was as follows:

|                            | Severance<br>and benefits<br>costs | Pension and<br>Retiree<br>Medical | Other exit<br>costs | Total    |
|----------------------------|------------------------------------|-----------------------------------|---------------------|----------|
| Balance at January 1, 2013 | \$62,540                           | \$—                               | \$5,218             | \$67,758 |
| Expenses, net              | 17,672                             | 1,964                             | 319                 | 19,955   |
| Cash payments              | (25,155)                           | —                                 | (2,100)             | (27,255) |
| Non-cash charges           | —                                  | (1,964)                           | —                   | (1,964)  |
| Balance at June 30, 2013   | \$55,057                           | \$—                               | \$3,437             | \$58,494 |

The majority of the remaining restructuring payments are expected to be paid through 2014; however, due to certain international labor laws and long-term lease agreements, some payments will extend beyond 2014. We expect that cash flows from operations will be sufficient to fund these payments.

## 7. Inventories

Inventories consisted of the following:

|                                    | June 30,<br>2013 | December 31,<br>2012 |
|------------------------------------|------------------|----------------------|
| Raw materials and work in process  | \$53,187         | \$66,221             |
| Supplies and service parts         | 65,478           | 72,551               |
| Finished products                  | 50,583           | 68,335               |
| Inventory at FIFO cost             | 169,248          | 207,107              |
| Excess of FIFO cost over LIFO cost | (28,187)         | (27,429)             |
| Total inventory, net               | \$141,061        | \$179,678            |

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 8. Intangible Assets and Goodwill

## Intangible assets

Intangible assets consisted of the following:

|                          | June 30, 2013         |                          |                     | December 31, 2012     |                          |                     |
|--------------------------|-----------------------|--------------------------|---------------------|-----------------------|--------------------------|---------------------|
|                          | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount |
| Customer relationships   | \$403,542             | \$(281,707 )             | \$121,835           | \$407,901             | \$(269,100 )             | \$138,801           |
| Supplier relationships   | 29,000                | (23,563 )                | 5,437               | 29,000                | (22,113 )                | 6,887               |
| Software & technology    | 167,598               | (153,294 )               | 14,304              | 169,632               | (151,628 )               | 18,004              |
| Trademarks & trade names | 34,582                | (32,748 )                | 1,834               | 35,078                | (32,615 )                | 2,463               |
| Non-compete agreements   | 7,288                 | (7,247 )                 | 41                  | 7,471                 | (7,412 )                 | 59                  |
| Total intangible assets  | \$642,010             | \$(498,559 )             | \$143,451           | \$649,082             | \$(482,868 )             | \$166,214           |

Amortization expense for intangible assets was \$9 million and \$11 million for the three months ended June 30, 2013 and 2012, respectively, and \$19 million and \$23 million for the six months ended June 30, 2013 and 2012, respectively. The future amortization expense for intangible assets as of June 30, 2013 was as follows:

|  |           |
|--|-----------|
| Remaining for year ended December 31, 2013 | \$19,035  |
| Year ended December 31, 2014               | 36,142    |
| Year ended December 31, 2015               | 32,376    |
| Year ended December 31, 2016               | 24,061    |
| Year ended December 31, 2017               | 11,359    |
| Thereafter                                 | 20,478    |
| Total                                      | \$143,451 |

Actual amortization expense may differ from the amounts above due to, among other things, fluctuations in foreign currency exchange rates, impairments, future acquisitions and accelerated amortization.

## Goodwill

As a result of lower than expected first half operating performance due to the loss of certain customer contracts, pricing pressure on contract renewals and a longer than originally anticipated sales cycle for some of our new growth areas in our North America Management Services operations (PBMS NA), future cash flows were estimated to be lower than originally projected. Given these factors, management determined that it was more likely than not that the fair value of the PBMS NA reporting unit was below its respective book value and, accordingly, it was necessary to perform an interim goodwill impairment test as of June 30, 2013.

The fair value of PBMS NA was determined based on a combination of techniques, including external valuation data, the present value of future cash flows and applicable multiples of competitors. Based on our review, the implied fair value of the goodwill was determined to be \$300 million compared to its carrying value of \$398 million, resulting in a charge of \$98 million. The inputs used to determine the fair value of PBMS NA were classified as Level 3 in the fair value hierarchy.

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

The changes in the carrying amount of goodwill, by reporting segment, for the six months ended June 30, 2013 were as follows:

|                                      | Gross value<br>before<br>accumulated<br>impairment | Accumulated<br>impairment | December 31,<br>2012 | Impairment<br>(2) | Other (1)  | June 30,<br>2013 |
|--------------------------------------|--|---------------------------|----------------------|-------------------|------------|------------------|
| North America Mailing                | \$355,874  | \$—                       | \$355,874            | \$—               | \$(2,980)  | \$352,894        |
| International Mailing                | 183,908  | —                         | 183,908              | —                 | (6,271)    | 177,637          |
| Small & Medium Business<br>Solutions | 539,782  | —                         | 539,782              | —                 | (9,251)    | 530,531          |
| Production Mail                      | 131,866  | —                         | 131,866              | —                 | (3,247)    | 128,619          |
| Software                             | 671,218  | —                         | 671,218              | —                 | (9,168)    | 662,050          |
| Management Services                  | 488,399  | (84,500)                  | 403,899              | (100,253)         | (1,467)    | 302,179          |
| Mail Services                        | 259,105  | (63,965)                  | 195,140              | —                 | —          | 195,140          |
| Marketing Services                   | 194,233  | —                         | 194,233              | —                 | —          | 194,233          |
| Enterprise Business Solutions        | 1,744,821  | (148,465)                 | 1,596,356            | (100,253)         | (13,882)   | 1,482,221        |
| Total                                | \$2,284,603  | \$(148,465)               | \$2,136,138          | \$(100,253)       | \$(23,133) | \$2,012,752      |

(1) Primarily foreign currency translation adjustments.

(2) Amount includes \$2 million impairment charge for PBMSi included in discontinued operations (see Note 4).

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 9. Debt

Debt consisted of the following:

|   | June 30,<br>2013 | December 31,<br>2012 |
|---|------------------|----------------------|
| Term loans                                | \$230,000        | \$230,000            |
| 3.875% notes due 2013                     | —                | 375,000              |
| 4.875% notes due 2014 <sup>(1), (2)</sup> | 299,570          | 450,000              |
| 5.0% notes due 2015 <sup>(1)</sup>        | 274,879          | 400,000              |
| 4.75% notes due 2016 <sup>(1)</sup>       | 370,914          | 500,000              |
| 5.75% notes due 2017                      | 500,000          | 500,000              |
| 5.60% notes due 2018                      | 250,000          | 250,000              |
| 4.75% notes due 2018                      | 350,000          | 350,000              |
| 6.25% notes due 2019                      | 300,000          | 300,000              |
| 5.25% notes due 2022                      | 110,000          | 110,000              |
| 5.25% notes due 2037                      | 500,000          | 500,000              |
| 6.70% notes due 2043 <sup>(3)</sup>       | 425,000          | —                    |
| Other <sup>(4)</sup>                      | 43,669           | 52,375               |
| Total debt                                | 3,654,032        | 4,017,375            |
| Current portion                           | —                | 375,000              |
| Long-term debt                            | \$3,654,032      | \$3,642,375          |

During the first quarter, we completed a cash tender offer (the Tender Offer) for a portion of our 4.875% Notes due 2014, our 5.0% Notes due 2015, and our 4.75% Notes due 2016 (the Subject Notes). Holders who validly tendered their notes received the principal amount of the notes tendered, all accrued and unpaid interest and a premium (1) amount. An aggregate \$405 million of the Subject Notes were tendered. A net loss of \$25 million, consisting of the payment of the call premium and transaction fees and the write-off of unamortized costs, partially offset by a gain from the unwinding of interest rate swap agreements, was recognized as Other expense, net on the Condensed Consolidated Statements of Income.

Prior to the Tender Offer, we had interest rate swap agreements with an aggregate notional value of \$450 million (2) that effectively converted the fixed rate interest payments on these notes into variable interest rates. As a result of the Tender Offer, we unwound \$225 million of these swap agreements.

During the first quarter, we issued \$425 million of 6.7% fixed rate 30-year notes. Interest is payable quarterly. The (3) notes mature in 2043, but may be redeemed, at our option, in whole or in part, at any time on or after March 7, 2018 at a redemption price equal to 100% of the principal amount, plus accrued and unpaid interest. The net proceeds from the notes were used to fund the Tender Offer.

(4) Other consists of the unamortized net proceeds received from unwinding of interest rate swaps, the mark-to-market adjustment of interest rate swaps and debt discounts and premiums.

In June 2013, the \$375 million 3.875% notes matured and were redeemed with cash.

At June 30, 2013, there were no outstanding commercial paper borrowings. During the quarter, commercial paper borrowings averaged \$75 million at a weighted-average interest rate of 0.46% and the maximum amount outstanding at any time was \$100 million.





## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 10. Noncontrolling Interests (Preferred Stockholders' Equity in Subsidiaries)

Pitney Bowes International Holdings, Inc. (PBIH), a subsidiary, has 300,000 shares, or \$300 million, of outstanding perpetual voting preferred stock (the Preferred Stock) held by certain institutional investors. The holders of the Preferred Stock are entitled as a group to 25% of the combined voting power of all classes of capital stock of PBIH. All outstanding common stock of PBIH, representing the remaining 75% of the combined voting power of all classes of capital stock, is owned directly or indirectly by the company. The Preferred Stock is entitled to cumulative dividends at a rate of 6.125% through 2016 after which it becomes callable and, if it remains outstanding, will yield a dividend that increases by 50% every six months thereafter. No dividends were in arrears at June 30, 2013 or December 31, 2012. There was no change in the carrying value of noncontrolling interests during the period ended June 30, 2013 or the year ended December 31, 2012.

## 11. Stockholders' Equity

Changes in stockholders' equity for the six months ended June 30, 2013 and 2012 were as follows:

|                                  | Preferred<br>stock | Preference<br>stock | Common<br>stock | Additional<br>paid-in<br>capital | Retained<br>earnings | Accumulated<br>other<br>comprehensiv<br>loss | Treasury<br>stock | Total<br>equity |
|----------------------------------|--------------------|---------------------|-----------------|----------------------------------|----------------------|--|-------------------|-----------------|
| Balance at January 1, 2013       | \$4                | \$ 648              | \$323,338       | \$223,847                        | \$4,744,802          | \$(681,213 )                                 | \$(4,500,795)     | \$110,631       |
| Net income                       | —                  | —                   | —               | —                                | 58,273               | —  | —                 | 58,273          |
| Other comprehensive income       | —                  | —                   | —               | —                                | —                    | (42,310 )                                    | —                 | (42,310 )       |
| Cash dividends                   |                    |                     |                 |                                  |                      |  |                   |                 |
| Common (\$0.5625 per share)      | —                  | —                   | —               | —                                | (113,083 )           | —  | —                 | (113,083 )      |
| Preference                       | —                  | —                   | —               | —                                | (23 )                | —  | —                 | (23 )           |
| Issuances of common stock        | —                  | —                   | —               | (31,532 )                        | —                    | —  | 33,144            | 1,612           |
| Conversions to common stock      | —                  | (35 )               | —               | (618 )                           | —                    | —  | 653               | —               |
| Stock-based compensation expense | —                  | —                   | —               | 7,241                            | —                    | —  | —                 | 7,241           |
| Balance at June 30, 2013         | \$4                | \$ 613              | \$323,338       | \$198,938                        | \$4,689,969          | \$(723,523 )                                 | \$(4,466,998)     | \$22,341        |
|                                  |                    |                     |                 |                                  |                      |  |                   |                 |
|                                  | Preferred<br>stock | Preference<br>stock | Common<br>stock | Additional<br>paid-in<br>capital | Retained<br>earnings | Accumulated<br>other<br>comprehensiv<br>loss | Treasury<br>stock | Total<br>equity |
| Balance at January 1, 2012       | \$4                | \$ 659              | \$323,338       | \$240,584                        | \$4,600,217          | \$(661,645 )                                 | \$(4,542,143)     | \$(38,986)      |
| Net income                       | —                  | —                   | —               | —                                | 258,293              | —  | —                 | 258,293         |
| Other comprehensive income       | —                  | —                   | —               | —                                | —                    | 3,987  | —                 | 3,987           |

|                                  |     |        |           |           |             |               |                |            |
|----------------------------------|-----|--------|-----------|-----------|-------------|---------------|----------------|------------|
| Cash dividends                   |     |        |           |           |             |               |                |            |
| Common (\$0.75 per share)        | —   | —      | —         | —         | (149,999 )  | —             | —              | (149,999 ) |
| Preference                       | —   | —      | —         | —         | (26 )       | —             | —              | (26 )      |
| Issuances of common stock        | —   | —      | —         | (22,176 ) | —           | —             | 21,321         | (855 )     |
| Conversions to common stock      | —   | (6 )   | —         | (124 )    | —           | —             | 130            | —          |
| Stock-based compensation expense | —   | —      | —         | 8,852     | —           | —             | —              | 8,852      |
| Balance at June 30, 2012         | \$4 | \$ 653 | \$323,338 | \$227,136 | \$4,708,485 | \$ (657,658 ) | \$ (4,520,692) | \$81,266   |

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 12. Accumulated Other Comprehensive Loss

Reclassifications out of accumulated other comprehensive income for the three and six months ended June 30, 2013 and 2012 was as follows:

|   | Amount Reclassified from AOCI (a) |              |                                |              |
|---|-----------------------------------|--------------|--------------------------------|--------------|
|   | Three Months Ended June 30, 2013  |              | Six Months Ended June 30, 2012 |              |
| Gains (losses) on cash flow hedges  |                                   |              |                                |              |
| Revenue   | \$ (371 )                         | \$ 473       | \$ (753 )                      | \$ 774       |
| Cost of sales   | 286                               | (7 )         | 412                            | (73 )        |
| Interest expense  | (507 )                            | (507 )       | (1,014 )                       | (1,014 )     |
| Total before tax  | (592 )                            | (41 )        | (1,355 )                       | (313 )       |
| Tax benefit   | 231                               | 17           | 528                            | 122          |
| Net of tax  | \$ (361 )                         | \$ (24 )     | \$ (827 )                      | \$ (191 )    |
| Unrealized gains (losses) on available for sale securities                    |                                   |              |                                |              |
| Interest income   | \$ 10                             | \$ (117 )    | \$ (2,602 )                    | \$ (476 )    |
| Tax benefit   | (3 )                              | 43           | 963                            | 176          |
| Net of tax  | \$ 7                              | \$ (74 )     | \$ (1,639 )                    | \$ (300 )    |
| Defined Benefit Pension Plans and Nonpension Postretirement Benefit Plans (b) |                                   |              |                                |              |
| Transition credit   | \$ 2                              | \$ 2         | \$ 4                           | \$ 4         |
| Prior service (costs) credit  | (163 )                            | 299          | (361 )                         | 589          |
| Actuarial losses  | (14,156 )                         | (18,347 )    | (31,902 )                      | (37,524 )    |
| Total before tax  | (14,317 )                         | (18,046 )    | (32,259 )                      | (36,931 )    |
| Tax benefit   | 4,926                             | 7,070        | 11,266                         | 13,967       |
| Net of tax  | \$ (9,391 )                       | \$ (10,976 ) | \$ (20,993 )                   | \$ (22,964 ) |

(a) Amounts in parentheses indicate debits (reductions) to income.

(b) These items are included in the computation of net periodic costs of defined benefit pension plans and nonpension postretirement benefit plans (see Note 15 for additional details).

Changes in accumulated other comprehensive income (AOCI) for the six months ended June 30, 2013 and 2012 were as follows:

|  | Gains (losses) on cash flow hedges | Unrealized gains (losses) on available for sale securities | Defined benefit pension plans and nonpension postretirement benefit plans | Foreign currency items | Total         |
|--|------------------------------------|--|---|------------------------|---------------|
| Balance at January 1, 2013   | \$ (7,777 )                        | \$ 4,513   | \$ (759,199 )   | \$ 81,250              | \$ (681,213 ) |
| Other comprehensive income (loss) before reclassifications (a)                 | 73                                 | (6,084 )   | —   | (62,317 )              | (68,328 )     |
| Amounts reclassified from accumulated other comprehensive income (a), (b), (c) | 827                                | 1,639  | 20,993  | 2,559                  | 26,018        |
|  | 900                                | (4,445 )   | 20,993  | (59,758 )              | (42,310 )     |

Net current period other comprehensive  
income

|                          |            |      |              |          |              |
|--------------------------|------------|------|--------------|----------|--------------|
| Balance at June 30, 2013 | \$(6,877 ) | \$68 | \$(738,206 ) | \$21,492 | \$(723,523 ) |
|--------------------------|------------|------|--------------|----------|--------------|

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## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

|  | Gains (losses)<br>on cash flow<br>hedges | Unrealized<br>gains (losses)<br>on available<br>for sale<br>securities | Defined benefit<br>pension plans<br>and nonpension<br>postretirement<br>benefit plans | Foreign<br>currency<br>items | Total        |
|--|--|--|---|------------------------------|--------------|
| Balance at January 1, 2012   | \$(8,438 )                               | \$4,387  | \$(741,546 )  | \$83,952                     | \$(661,645 ) |
| Other comprehensive income (loss)<br>before reclassifications (a)            | 362                                      | 78   | —   | (19,908 )                    | (19,468 )    |
| Amounts reclassified from accumulated<br>other comprehensive income (a), (b) | 191                                      | 300  | 22,964  | —                            | 23,455       |
| Net current period other comprehensive<br>income                             | 553                                      | 378  | 22,964  | (19,908 )                    | 3,987        |
| Balance at June 30, 2012   | \$(7,885 )                               | \$4,765  | \$(718,582 )  | \$64,044                     | \$(657,658 ) |

(a) Amounts are net of tax. Amounts in parentheses indicate debits to AOCI.

(b) See table above for additional details of these reclassifications.

Foreign currency item amount represents the recognition of deferred translation upon the sale of the U.K. IMS (c)business. Amount was reclassified from accumulated other comprehensive loss and recorded as discontinued operations in the Condensed Consolidated Statements of Income.

## 13. Income Taxes

The effective tax rate for the three months ended June 30, 2013 and 2012 was 49.6% and 33.0%, respectively. The effective tax rate for the six months ended June 30, 2013 and 2012 was 32.0% and 21.3%, respectively. The effective tax rate for the three and six months ended June 30, 2013 includes tax benefits of \$7 million related to one-time tax planning initiatives and \$4 million from the adjustment of non-U.S. tax accounts from prior periods offset by the reduced tax benefits associated with the goodwill impairment charge. The effective tax rate for the 2013 year-to-date period also includes a benefit of \$4 million from the retroactive effect of 2013 U.S. tax legislation. The effective tax rate for the six months ended June 30, 2012 includes tax benefits of \$17 million from the sale of non-U.S. leveraged lease assets and \$22 million from the resolution of tax examinations.

As is the case with other large corporations, our tax returns are examined each year by tax authorities in the U.S., other countries and local jurisdictions in which we have operations. We expect the examination of our 2009 through 2011 tax returns by the Internal Revenue Service (IRS) to be completed within the next 12 months. We regularly assess the likelihood of tax adjustments in each of the tax jurisdictions in which we do business and account for the related financial statement implications. We believe we have established tax reserves that are appropriate given the possibility of tax adjustments. However, determining the appropriate level of tax reserves requires judgment regarding the uncertain application of tax law and the possibility of tax adjustments. Future changes in tax reserve requirements could have a material impact, positive or negative, on our results of operations, financial position and cash flows. It is reasonably possible that the amount of our unrecognized tax benefits will decrease in the next 12 months, and we expect this change could be up to twenty percent of our unrecognized tax benefits.

On August 27, 2012, the United States Court of Appeals for the Third Circuit overturned a prior Tax Court decision and ruled in favor of the IRS and adverse to the Historic Boardwalk Hall LLC, a partnership in which we had made an investment in the year 2000. During the quarter, the U.S. Supreme Court decided not to hear the partnership's appeal of the Third Circuit decision, and the case has since been sent back to the Tax Court for additional proceedings. Based on our entitlement to indemnification under the partnership agreement, we do not expect this matter to have a material effect on our results of operations. However, the potential for a difference in the timing of payments which may be due to taxing authorities and the timing of receipts due to us under the partnership agreement may cause fluctuations in our cash flows in future periods.

## 14. Commitments and Contingencies

In the ordinary course of business, we are routinely defendants in, or party to a number of pending and threatened legal actions. These may involve litigation by or against us relating to, among other things, contractual rights under vendor, insurance or other contracts; intellectual property or patent rights; equipment, service, payment or other disputes with customers; or disputes with employees. Some of these actions may be brought as a purported class action on behalf of a purported class of employees, customers or others.

In October 2009, the company and certain of its current and former officers were named as defendants in NECA-IBEW Health & Welfare Fund v. Pitney Bowes Inc. et al., a class action lawsuit filed in the U.S. District Court for the District of Connecticut. The complaint asserts claims under the Securities Exchange Act of 1934 on behalf of those who purchased the common stock of the company during the period between July 30, 2007 and October 29, 2007 alleging that the company, in essence, missed two financial projections. Plaintiffs filed an amended complaint in September 2010. On March 23, 2013, the Court granted our motion to dismiss, and dismissed the case in its entirety. Plaintiff did not appeal the decision, and therefore, this case has now concluded in favor of Pitney Bowes and its officers named in the lawsuit.

## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 15. Pensions and Other Benefit Programs

## Defined Benefit Pension Plans

The components of net periodic benefit cost for defined benefit pension plans were as follows:

|                                    | Three Months Ended June 30, |           |           |           |
|------------------------------------|-----------------------------|-----------|-----------|-----------|
|                                    | United States               |           | Foreign   |           |
|                                    | 2013                        | 2012      | 2013      | 2012      |
| Service cost                       | \$3,494                     | \$4,515   | \$2,139   | \$2,013   |
| Interest cost                      | 18,534                      | 19,917    | 11,627    | 6,934     |
| Expected return on plan assets     | (27,041 )                   | (30,194 ) | (13,886 ) | (8,041 )  |
| Amortization of transition credit  | —                           | —         | (2 )      | (2 )      |
| Amortization of prior service cost | 94                          | 197       | 28        | 27        |
| Amortization of net actuarial loss | 7,507                       | 13,165    | 4,290     | 3,492     |
| Settlement                         | 1,416                       | —         | —         | 250       |
| Special termination benefits       | 548                         | —         | —         | —         |
| Net periodic benefit cost          | \$4,552                     | \$7,600   | \$4,196   | \$4,673   |
|                                    | Six Months Ended June 30,   |           |           |           |
|                                    | United States               |           | Foreign   |           |
|                                    | 2013                        | 2012      | 2013      | 2012      |
| Service cost                       | \$7,293                     | \$9,469   | \$4,312   | \$4,031   |
| Interest cost                      | 36,905                      | 40,520    | 23,376    | 13,857    |
| Expected return on plan assets     | (54,127 )                   | (60,812 ) | (27,921 ) | (16,064 ) |
| Amortization of transition credit  | —                           | —         | (4 )      | (4 )      |
| Amortization of prior service cost | 223                         | 402       | 56        | 55        |
| Amortization of net actuarial loss | 18,544                      | 26,479    | 8,638     | 6,988     |
| Settlement                         | 1,416                       | —         | —         | 250       |
| Special termination benefits       | 548                         | —         | —         | —         |
| Curtailement                       | 814                         | —         | —         | —         |
| Net periodic benefit cost          | \$11,616                    | \$16,058  | \$8,457   | \$9,113   |

Through June 30, 2013, we contributed \$7 million to our U.S. pension plans and \$7 million to our foreign pension plans.

## Nonpension Postretirement Benefit Plans

The components of net periodic benefit cost for nonpension postretirement benefit plans were as follows:

|   | Three Months Ended June 30, |         | Six Months Ended June 30, |          |
|---|-----------------------------|---------|---------------------------|----------|
|   | 2013                        | 2012    | 2013                      | 2012     |
|   | Service cost                | \$1,014 | \$868                     | \$2,031  |
| Interest cost                               | 2,510                       | 2,714   | 5,024                     | 5,789    |
| Amortization of prior service cost (credit) | 41                          | (523 )  | 82                        | (1,046 ) |
| Amortization of net actuarial loss          | 2,359                       | 1,690   | 4,720                     | 4,057    |
| Net periodic benefit cost                   | \$5,924                     | \$4,749 | \$11,857                  | \$10,559 |

Contributions for benefit payments for our nonpension postretirement benefit plans were \$8 million for each of the three months ended June 30, 2013 and 2012, respectively, and \$16 million and \$14 million for the six months ended June 30, 2013 and 2012, respectively.





## PITNEY BOWES INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

## 16. Earnings per Share

The calculations of basic and diluted earnings per share are presented below:

|  | Three Months Ended June 30, |           | Six Months Ended June 30, |           |
|--|-----------------------------|-----------|---------------------------|-----------|
|  | 2013                        | 2012      | 2013                      | 2012      |
| Numerator:   |                             |           |                           |           |
| Amounts attributable to common stockholders:   |                             |           |                           |           |
| Net income from continuing operations  | \$10,834                    | \$103,435 | \$82,029                  | \$243,447 |
| (Loss) income from discontinued operations   | (20,067 )                   | (3,812 )  | (23,756 )                 | 14,846    |
| Net (loss) income - Pitney Bowes Inc. (numerator for diluted EPS)                            | (9,233 )                    | 99,623    | 58,273                    | 258,293   |
| Less: Preference stock dividend  | (13 )                       | (13 )     | (23 )                     | (26 )     |
| (Loss) income attributable to common stockholders (numerator for basic EPS)                  | \$(9,246 )                  | \$99,610  | \$58,250                  | \$258,267 |
| Denominator (in thousands):  |                             |           |                           |           |
| Weighted-average shares used in basic EPS  | 201,567                     | 200,252   | 201,342                   | 200,091   |
| Effect of dilutive shares:   |                             |           |                           |           |
| Preferred stock  | 2                           | 2         | 2                         | 2         |
| Preference stock   | 387                         | 398       | 390                       | 399       |
| Stock plans  | 847                         | 459       | 646                       | 407       |
| Weighted-average shares used in diluted EPS  | 202,803                     | 201,111   | 202,380                   | 200,899   |
| Basic earnings per share:  |                             |           |                           |           |
| Continuing operations  | \$0.05                      | \$0.52    | \$0.41                    | \$1.22    |
| Discontinued operations  | (0.10 )                     | (0.02 )   | (0.12 )                   | 0.07      |
| Net (loss) income  | \$(0.05 )                   | \$0.50    | \$0.29                    | \$1.29    |
| Diluted earnings per share:  |                             |           |                           |           |
| Continuing operations  | \$0.05                      | \$0.51    | \$0.41                    | \$1.21    |
| Discontinued operations  | (0.10 )                     | (0.02 )   | (0.12 )                   | 0.07      |
| Net (loss) income  | \$(0.05 )                   | \$0.50    | \$0.29                    | \$1.29    |
| Anti-dilutive shares not used in calculating diluted weighted-average shares (in thousands): | 12,673                      | 13,737    | 12,881                    | 14,517    |

PITNEY BOWES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited; table amounts in thousands of dollars, unless otherwise noted)

17. Subsequent Event

On July 30, 2013, we entered into a Stock and Asset Purchase Agreement (Purchase Agreement) to sell PBMS NA to an affiliate of Apollo Global Management, LLC for \$400 million in cash consideration, subject to post-closing purchase price adjustments, as defined in the Purchase Agreement. We estimate that we will incur approximately \$8 million of transaction fees and expenses related to this transaction. Completion of the sales transaction is subject to customary closing conditions, and is expected to close in the fourth quarter.

The sale of this business is part of our current transformation strategy to improve the growth profile and profitability of our company. Together with the International Management Services operations that were sold, or are in the process of being sold (see Note 4), our worldwide Management Services operations contributed \$921 million, or 19%, of our reported consolidated revenue and \$37 million, or 8%, of our reported consolidated net income for the year ended December 31, 2012.

In the third quarter, the results of PBMS NA will be reported as a discontinued operation, and we expect to incur a charge in the range of \$80 to \$100 million, or \$0.40 to \$0.50 per share, primarily resulting from a tax gain attributable to the difference between the company's book and tax basis in this business. This estimated charge is subject to post-closing purchase price adjustments, as defined in the Purchase Agreement.

Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations  
Forward-Looking Statements

This Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) contains statements that are forward-looking. We want to caution readers that any forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act) and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act) in this Form 10-Q may change based on various factors. These forward-looking statements are based on current expectations and assumptions that are subject to risks and uncertainties and actual results could differ materially. Words such as "estimate", "target", "project", "plan", "believe", "expect", "anticipate", "intend", and similar expressions may identify such forward-looking statements. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Factors which could cause future financial performance to differ materially from the expectations as expressed in any forward-looking statement made by or on our behalf include, without limitation:

- declining physical mail volumes
- mailers' utilization of alternative means of communication or competitors' products
- access to capital at a reasonable cost to continue to fund various discretionary priorities, including business investments, pension contributions and dividend payments
- timely development and acceptance of new products and services
- successful entry into new markets
- success in gaining product approval in new markets where regulatory approval is required
- changes in postal or banking regulations
- interrupted use of key information systems
- third-party suppliers' ability to provide product components, assemblies or inventories
- our success at managing the relationships with our outsource providers, including the costs of outsourcing functions and operations not central to our business
- changes in privacy laws
- intellectual property infringement claims
- regulatory approvals and satisfaction of other conditions to consummate and integrate any acquisitions
- negative developments in economic conditions, including adverse impacts on customer demand
- our success at managing customer credit risk
- significant changes in pension, health care and retiree medical costs
- changes in interest rates, foreign currency fluctuations or credit ratings
- income tax adjustments or other regulatory levies for prior audit years and changes in tax laws, rulings or regulations
- impact on mail volume resulting from concerns over the use of the mail for transmitting harmful biological agents
- changes in international or national political conditions, including any terrorist attacks
- acts of nature

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our Condensed Consolidated Financial Statements contained in this report and our Annual Report to Stockholders on Form 10-K for the year ended December 31, 2012 (2012 Annual Report).

Overview

For the second quarter of 2013, revenue decreased 1% to \$1,158 million compared to \$1,166 million in the second quarter of 2012. Equipment sales and supplies revenue increased 9% and 3%, respectively, primarily due to the installation of large production print and inserting equipment in North America during the quarter. Offsetting these increases was a 4% decline in software revenue due to fewer large dollar value licensing deals and continued weakness in our international markets, in part, due to constrained public sector spending; a 6% decline in rental revenue due to fewer installed meters worldwide; a 6% decline in financing revenue due to the impact of lower equipment sales in prior periods; and a 5% decline in support services revenue due to lower new equipment

placements. Foreign currency translation had a less than 1% unfavorable impact on revenue in the quarter.

Net income from continuing operations attributable to common stockholders decreased to \$11 million, or \$0.05 per diluted share in the second quarter of 2013 compared to \$103 million or \$0.51 per diluted share in the second quarter of 2012, primarily due to a pretax goodwill impairment charge of \$0.40 per diluted share and restructuring charges of \$0.07 per diluted share. See "Restructuring charges" and "Goodwill impairment" in the Results of Operations section of this MD&A for further details of these charges.

As part of our current transformation strategy to improve the growth profile and profitability of our company, during the quarter, we entered into two separate agreements to sell our International Management Services operations (PBMSi). The assets and liabilities of

PBMSi met held-for-sale classification and all amounts are presented as discontinued operations for all periods presented in the Condensed Consolidated Statements of Income. The operating results of PBMSi were previously included in our Management Services segment. We closed on one of the agreements on July 5, 2013 and expect to close on the second agreement by the end of the third quarter. Total proceeds from these sales will not be material.

Additionally, on July 30, 2013, we entered into a definitive agreement to sell our North America Management Services operations (PBMS NA) to an affiliate of Apollo Global Management, LLC for \$400 million in cash consideration, subject to post-closing purchase price adjustments. We estimate that we will incur approximately \$8 million of transaction fees and expenses related to this transaction. Completion of the sales transaction is subject to customary closing conditions, and is expected to close in the fourth quarter. Proceeds from the sale will be used primarily to reduce debt.

While our worldwide Management Services business (PBMSi and PBMS NA, collectively PBMS) contributed a significant amount of revenue, its contribution to our profitability was not as significant. For the year ended December 31, 2012, PBMS contributed \$921 million, or 19%, of our reported consolidated revenue, but only \$37 million, or 8%, of our reported consolidated net income. Total assets of PBMS at December 31, 2012 were \$701 million.

In the third quarter, the results of PBMS NA will be reported as a discontinued operation, and we expect to incur a charge in the range of \$80 to \$100 million, or \$0.40 to \$0.50 per share, primarily resulting from a tax gain attributable to the difference between the company's book and tax basis in this business. This estimated charge is subject to post-closing purchase price adjustments, as defined in the Purchase Agreement.

#### Outlook

Worldwide economic weakness continues to create a challenging business environment causing many of our customers to remain cautious about spending and, therefore, impacting the performance of our business segments. Small and Medium Business Solutions (SMB) revenues continue to be challenged by the decline in physical mail volumes as alternative means of communications evolve and gain further acceptance. However, historical trends for equipment sales and recurring revenue streams are beginning to show some improvement, and we expect this improvement to continue during the second half of the year, due in part to global sales of our Connect+™ communications systems and SendSuite Live™ shipping solutions.

We anticipate revenue growth in certain of our Enterprise Business Solutions segments from continued expansion in our Mail Services presort operations, new ecommerce initiatives and market acceptance for our new solutions that help customers grow their business by more effectively managing their physical and digital communications with their customers. We will continue to fund investments to build capacity and infrastructure to support our ecommerce products and solutions. We are also committed to improving the performance of our Software business and expect revenue and profitability improvements as a result of our recently appointed new leadership, a re-alignment of our sales force and initiatives focused on improving the cost structure.

Our growth strategies will focus on leveraging our expertise in physical communications with our expanding capabilities in digital and hybrid communications. We will continue to develop and invest in products, software, services and solutions that help customers grow their business by more effectively communicating with their customers across physical, digital and hybrid channels. We expect our mix of business will continue to shift to more enterprise related products and solutions, and that these new revenue streams will have lower margins than our traditional mailing business.



## RESULTS OF OPERATIONS

Revenue by source and the related cost of revenue are shown in the following tables:

## Revenue

| (\$ amounts in 000s) | Three Months Ended June 30, |             |          | Six Months Ended June 30, |             |          |
|----------------------|-----------------------------|-------------|----------|---------------------------|-------------|----------|
|                      | 2013                        | 2012        | % change | 2013                      | 2012        | % change |
| Equipment sales      | \$243,644                   | \$224,235   | 9 %      | \$458,643                 | \$444,414   | 3 %      |
| Supplies             | 72,337                      | 70,522      | 3 %      | 146,624                   | 146,887     | — %      |
| Software             | 100,482                     | 104,551     | (4) %    | 187,494                   | 208,901     | (10) %   |
| Rentals              | 136,775                     | 145,497     | (6) %    | 273,154                   | 285,886     | (4) %    |
| Financing            | 115,929                     | 122,948     | (6) %    | 232,691                   | 249,696     | (7) %    |
| Support services     | 163,178                     | 171,254     | (5) %    | 328,664                   | 344,772     | (5) %    |
| Business services    | 325,862                     | 327,350     | — %      | 649,207                   | 655,447     | (1) %    |
| Total revenue        | \$1,158,207                 | \$1,166,357 | (1) %    | \$2,276,477               | \$2,336,003 | (3) %    |

## Cost of revenue

| (\$ amounts in 000s)       | Three Months Ended June 30, |           |                       |        | Six Months Ended June 30, |             |                       |        |
|----------------------------|-----------------------------|-----------|-----------------------|--------|---------------------------|-------------|-----------------------|--------|
|                            | 2013                        | 2012      | Percentage of Revenue |        | 2013                      | 2012        | Percentage of Revenue |        |
| Cost of equipment sales    | \$128,426                   | \$106,718 | 52.7 %                | 47.6 % | \$237,763                 | \$203,634   | 51.8 %                | 45.8 % |
| Cost of supplies           | 22,692                      | 20,863    | 31.4 %                | 29.6 % | 45,954                    | 44,734      | 31.3 %                | 30.5 % |
| Cost of software           | 21,435                      | 24,404    | 21.3 %                | 23.3 % | 42,141                    | 45,497      | 22.5 %                | 21.8 % |
| Cost of rentals            | 26,424                      | 31,851    | 19.3 %                | 21.9 % | 54,179                    | 62,076      | 19.8 %                | 21.7 % |
| Financing interest expense | 19,798                      | 20,642    | 17.1 %                | 16.8 % | 39,673                    | 41,781      | 17.0 %                | 16.7 % |
| Cost of support services   | 104,282                     | 112,123   | 63.9 %                | 65.5 % | 212,291                   | 227,210     | 64.6 %                | 65.9 % |
| Cost of business services  | 248,715                     | 242,010   | 76.3 %                | 73.9 % | 495,611                   | 485,952     | 76.3 %                | 74.1 % |
| Total cost of revenue      | \$571,772                   | \$558,611 | 49.4 %                | 47.9 % | \$1,127,612               | \$1,110,884 | 49.5 %                | 47.6 % |

## Equipment sales

Equipment sales revenue increased 9% to \$244 million and 3% to \$459 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2012. The increase in equipment sales was driven primarily by the installation of large production print and inserting equipment in North America, but also benefited from increased sales of Connect+™ mailing systems in Europe. Equipment sales in our North America mailing business declined 5% in the quarter and 7% in the year-to-date period compared to the prior year periods mainly due to declining mail volumes. Equipment sales for the year-to-date period also included revenue of \$3 million for scale updates resulting from a postal rate change in France. Cost of equipment sales as a percentage of revenue increased to 52.7% in the quarter and 51.8% in the year-to-date period compared to 47.6% and 45.8% in the same periods in 2012, respectively, primarily due to a higher mix of lower margin product sales.

## Supplies

Supplies revenue increased 3% to \$72 million and was flat at \$147 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2012. The increase in the quarter was mainly due to supply sales related to the installation of production print equipment in the quarter and the growing base of production print equipment installations. Year-to-date supplies revenue was flat compared to the prior year-to-date period as increased supply sales for production print equipment and Connect+™ mailing systems in Europe were offset by lower supply sales in



our North America mailing business due to reduced mail volumes and fewer installed meters. Cost of supplies as a percentage of revenue increased to 31.4% in the quarter and 31.3% in the year-to-date period compared to 29.6% and 30.5% in the same periods in 2012, respectively, due to reduced margins on supplies sales.

Software

Software revenue decreased 4% to \$100 million and 10% to \$187 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2012 primarily due to fewer large dollar licensing contracts in our North America markets, and uncertain economic

conditions and constrained public sector spending in our international markets. Cost of software as a percentage of revenue improved to 21.3% in the quarter compared with 23.3% in the prior year quarter as cost reduction initiatives more than offset the impact on margin from lower revenue. For the year-to-date period, cost of software as a percentage of revenue increased to 22.5% compared to 21.8% in the prior year period primarily due to the decline in revenue.

#### Rentals

Rentals revenue decreased 6% to \$137 million and 4% to \$273 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2012, primarily due to lower mail volumes and fewer meters in service. Cost of rentals as a percentage of revenue improved to 19.3% and 19.8% in the quarter and year-to-date periods, respectively, compared to 21.9% and 21.7% in the prior year periods primarily due to lower depreciation expense.

#### Financing

Financing revenue decreased 6% to \$116 million and 7% to \$233 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2012, primarily due to lower equipment sales in prior periods. Financing interest expense as a percentage of revenue for the quarter and year-to-date periods increased to 17.1% and 17.0%, respectively, compared to 16.8% and 16.7% in the comparable prior year periods due to higher effective interest rates. In computing our financing interest expense, which represents our cost of borrowing associated with the generation of financing revenue, we assume a 10:1 leveraging ratio of debt to equity and apply our overall effective interest rate to the average outstanding finance receivables.

#### Support Services

Support services revenue decreased 5% in both the quarter and year-to-date periods to \$163 million and \$329 million, respectively, compared to the same periods in 2012, primarily driven by lower new equipment placements worldwide. Cost of support services as a percentage of revenue improved to 63.9% and 64.6% in the quarter and year-to-date periods, respectively, compared to 65.5% and 65.9% in the prior year periods due to productivity initiatives in our International Mailing business.

#### Business Services

Business services revenue was flat for the quarter at \$326 million and decreased 1% in the year-to-date period to \$649 million compared to the same periods in 2012. The quarter and year-to-date periods benefited from revenue from our ecommerce solutions for cross-border package delivery and higher standard and first-class mail volumes; however, these benefits were offset by lost business and pricing pressure in our Management Services business and lower fees under certain contract renewals in our Marketing Services business. Cost of business services as a percentage of revenue was 76.3% in both the quarter and year-to-date periods compared to 73.9% and 74.1% in the same periods in 2012, respectively. The increase was primarily due to margin compression in our Management Services business and continuing investment in the growth of our ecommerce offering.

#### Selling, general and administrative (SG&A)

SG&A expense decreased 1% to \$377 million in the quarter and 4% to \$748 million in the year-to-date period compared to the same periods in 2012 driven primarily by lower salaries and benefits and other cost reduction initiatives.

#### Restructuring charges and asset impairments

In order to enhance our responsiveness to changing market conditions, further streamline our business operations, reduce our cost structure and create long-term flexibility to invest in growth, we have identified certain actions that we believe will provide both process and operational improvements. We anticipate that these primarily cash related actions will result in restructuring charges in the range of \$75 to \$125 million and will be recognized as specific initiatives are approved and implemented. We anticipate annualized pre-tax benefits of \$100 to \$125 million, net of investments, from these actions, and expect to reach this benefit run rate by 2015.

During the quarter, we began implementing certain actions, consisting primarily of workforce reductions, and recorded restructuring charges of \$23 million in connection with the above actions. Restructuring charges for the

period also include the reversal of \$3 million for changes in reserves under prior restructuring programs.

#### Goodwill impairment

Goodwill is tested for impairment annually during the fourth quarter, or sooner when circumstances indicate an impairment may exist at the reporting unit level. The impairment test for goodwill is a two-step approach. In the first step, the fair value of each reporting unit is compared to the reporting unit's carrying value, including goodwill. If the fair value of a reporting unit is less than its carrying value, the second step of the goodwill impairment test is performed to measure the amount of impairment, if any. In the second step, the fair value of the reporting unit is allocated to the assets and liabilities of the reporting unit as if it had been acquired in a business combination and the purchase price was equivalent to the fair value of the reporting unit. The excess of the fair value of the reporting unit over the amounts assigned to its assets and liabilities is referred to as the implied fair value of goodwill. The implied fair value of the reporting

unit's goodwill is then compared to the actual carrying value of goodwill. If the implied fair value of goodwill is less than the carrying value of goodwill, an impairment loss is recognized for the difference.

As a result of lower than expected first half operating performance due to the loss of certain customer contracts, continued pricing pressure on contract renewals and a longer than originally anticipated sales cycle for some of our new growth areas in PBMS NA, future near-term cash flows are estimated to be lower than originally projected. Accordingly, management determined that it was necessary to perform a goodwill impairment review as of June 30, 2013. The fair value of PBMS NA was determined based on a combination of techniques, including external valuation data, the present value of future cash flows and applicable multiples of competitors. The inputs used to determine the fair value of PBMS NA were classified as Level 3 in the fair value hierarchy. Based on our review, a goodwill impairment charge of \$98 million was recorded.

Significant estimates and assumptions are used in determining the fair value of each reporting unit regarding discount rates, growth rates and our future long-term business plans. Changes in any of these estimates or assumptions could materially affect the determination of fair value and the associated goodwill impairment charge for each reporting unit.

#### Other expense, net

Other expense, net for the six months ended June 30, 2013 of \$25 million consists of the costs associated with the early redemption of debt during the first quarter. See Liquidity and Capital Resources - Financings and Capitalization for a detailed discussion.

Other expense, net for the three and six months ended June 30, 2012 was comprised of the following:

|  | (Income) / Expense                     |                                      |
|--|--|--------------------------------------|
|  | Three months<br>ended June<br>30, 2012 | Six months<br>ended June<br>30, 2012 |
| Insurance proceeds                                   | \$(4                                   | ) \$(11                              |
| Loss on forward starting swap agreement              | 6                                      | 6                                    |
| Early termination of debt, net                       | 2                                      | 2                                    |
| Pretax loss on sale of certain leverage lease assets | —                                      | 4                                    |
| Other expense, net                                   | \$4                                    | \$1                                  |

Insurance proceeds were received in connection with the 2011 fire at our Dallas presort facility.

In April 2012, we entered into forward starting swap agreements to hedge interest rate risk associated with a forecasted issuance of long-term debt. Our anticipated debt issuance did not occur prior to the expiration of these swap agreements, resulting in a loss of \$6 million.

In connection with the early redemption of \$400 million, 4.625% notes (the 2012 Notes) in June 2012, we incurred a net loss of \$2 million consisting of a \$4 million make-whole payment offset by a gain of \$2 million associated with the termination of interest rate swap contracts related to the 2012 Notes.

In the first quarter of 2012, we completed a sale of certain non-U.S. leveraged lease assets to the lessee for cash and incurred a pretax loss of \$4 million.

#### Income taxes

See Note 13 to the unaudited Condensed Consolidated Financial Statements.

#### Discontinued operations

See Note 4 to the unaudited Condensed Consolidated Financial Statements.

#### Preferred stock dividends of subsidiaries attributable to noncontrolling interests

See Note 10 to the unaudited Condensed Consolidated Financial Statements.



### Business segment results

We conduct our business activities in seven reporting segments within two business groups, Small & Medium Business Solutions and Enterprise Business Solutions. The following tables show revenue and EBIT by business segment for the three and six months ended June 30, 2013 and 2012. We determine segment EBIT, a non-GAAP measure, by deducting from segment revenue the related costs and expenses attributable to the segment. Segment EBIT excludes interest, taxes, general corporate expenses, restructuring charges and impairment charges, which are not allocated to a particular business segment. Management uses segment EBIT to measure profitability and performance at the segment level. Management presents segment EBIT because it believes segment EBIT provides investors with an analysis of the company's operating performance and underlying trends of the businesses. Segment EBIT may not be indicative of our overall consolidated performance and therefore, should be read in conjunction with our condensed consolidated results of operations. Refer to Note 2 to the Condensed Consolidated Financial Statements for a reconciliation of segment EBIT to income from continuing operations before income taxes.

Certain amounts in the tables below have been revised to reflect our International Mailing Services (IMS) operations and PBMSi as discontinued operations. IMS was previously included in our Mail Services segment and PBMSi was previously included in our Management Services segment.

| Revenue<br>(\$ amounts in 000s)   | Three Months Ended June 30, |             |          | Six Months Ended June 30, |             |          |
|-----------------------------------|-----------------------------|-------------|----------|---------------------------|-------------|----------|
|                                   | 2013                        | 2012        | % change | 2013                      | 2012        | % change |
| North America Mailing             | \$432,889                   | \$453,484   | (5)%     | \$863,264                 | \$914,789   | (6)%     |
| International Mailing             | 164,556                     | 165,480     | (1)%     | 332,011                   | 333,494     | —%       |
| Small & Medium Business Solutions | 597,445                     | 618,964     | (3)%     | 1,195,275                 | 1,248,283   | (4)%     |
| Production Mail                   | 144,986                     | 123,067     | 18%      | 263,788                   | 238,083     | 11%      |
| Software                          | 92,242                      | 99,874      | (8)%     | 172,963                   | 200,201     | (14)%    |
| Management Services               | 174,708                     | 180,562     | (3)%     | 351,278                   | 360,702     | (3)%     |
| Mail Services                     | 119,058                     | 108,045     | 10%      | 237,913                   | 222,681     | 7%       |
| Marketing Services                | 29,768                      | 35,845      | (17)%    | 55,260                    | 66,053      | (16)%    |
| Enterprise Business Solutions     | 560,762                     | 547,393     | 2%       | 1,081,202                 | 1,087,720   | (1)%     |
| Total                             | \$1,158,207                 | \$1,166,357 | (1)%     | \$2,276,477               | \$2,336,003 | (3)%     |
| EBIT<br>(\$ amounts in 000s)      | Three Months Ended June 30, |             |          | Six Months Ended June 30, |             |          |
|                                   | 2013                        | 2012        | % change | 2013                      | 2012        | % change |
| North America Mailing             | \$166,363                   | \$167,870   | (1)%     | \$320,868                 | \$346,041   | (7)%     |
| International Mailing             | 19,285                      | 21,758      | (11)%    | 37,034                    | 41,755      | (11)%    |
| Small & Medium Business Solutions | 185,648                     | 189,628     | (2)%     | 357,902                   | 387,796     | (8)%     |
| Production Mail                   | 13,617                      | 5,594       | 143%     | 16,672                    | 8,373       | 99%      |
| Software                          | 15,729                      | 8,487       | 85%      | 20,619                    | 19,179      | 8%       |
| Management Services               | 14,735                      | 14,222      | 4%       | 29,097                    | 26,210      | 11%      |
| Mail Services                     | 15,484                      | 28,464      | (46)%    | 34,833                    | 62,709      | (44)%    |
| Marketing Services                | 4,181                       | 7,503       | (44)%    | 6,167                     | 12,320      | (50)%    |
| Enterprise Business Solutions     | 63,746                      | 64,270      | (1)%     | 107,388                   | 128,791     | (17)%    |
| Total                             | \$249,394                   | \$253,898   | (2)%     | \$465,290                 | \$516,587   | (10)%    |

#### Small & Medium Business Solutions

Small & Medium Business Solutions revenue for the quarter and year-to-date periods decreased 3% and 4% to \$597 million and \$1,195 million, respectively, compared to the same periods in 2012. EBIT for the quarter and year-to-date periods decreased 2% and 8% to \$186 million and \$358 million, respectively, compared to the same periods in 2012.

#### North America Mailing

Revenue for the North America Mailing segment decreased 5% to \$433 million and 6% to \$863 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2012. Compared to the prior year, equipment sales declined 5% in the quarter and 7% in the year-to-date period mainly due to declining mail volumes and continued concerns about economic conditions. Financing revenue



declined 7% in the quarter and 8% in the year-to-date period due to declining equipment sales in prior periods. Rentals revenue declined 5% in the quarter and 4% in the year-to-date period primarily due to fewer meters in service and supplies revenue declined 2% in the quarter and 4% in the year-to-date period primarily due to lower mail volumes and a declining installed meter base.

EBIT decreased 1% to \$166 million in the quarter compared to the prior year quarter primarily due to the decline in revenue; however, EBIT margin improved due to cost reduction initiatives. EBIT for the year-to-date period decreased 7% to \$321 million compared to the prior year period primarily due to the decline in revenue.

#### International Mailing

Revenue for the International Mailing segment for the quarter decreased 1% to \$165 million and less than 1% to \$332 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2012. Compared to the prior year, rental revenue declined 14% in the quarter and 9% in the year-to-date period driven primarily by lower rental revenue in France due to the effect of a change in mix from rentals to equipment sales in 2012 and lower rental revenue in the U.K. due to fewer installed meters. Offsetting this decline was higher financing revenue of 4% in the quarter and 5% in the year-to-date period due to positive equipment sales in prior periods, driven primarily by the change in mix from rentals to equipment sales in France in 2012, and higher sales in the Nordics. Equipment sales increased 3% in the quarter and 1% in the year-to-date period higher sales in the Nordics and increased sales of our Connect+™ mailing systems in Germany, partially offset by lower equipment sales in the U.K. due to the continuing uncertain economic environment. Year-to-date equipment sales also benefited from revenue for scale updates resulting from a postal rate change in France. Supplies revenue was up 2% in the quarter due to higher sales in Asia-Pacific, but flat compared to the year-to-date period.

EBIT decreased 11% in both the quarter and year-to-date periods to \$19 million and \$37 million, respectively, compared to the same periods in 2012 primarily due to lower margin equipment sales and costs related to facilities consolidation.

#### Enterprise Business Solutions

Enterprise Business Solutions revenue for the quarter increased 2% to \$561 million and EBIT decreased 1% to \$64 million, compared to the prior year quarter. For the year-to-date period, revenue decreased 1% to \$1,081 million and EBIT decreased 17% to \$107 million compared to the prior year-to-date period.

#### Production Mail

Revenue for the Production Mail segment increased 18% to \$145 million and 11% to \$264 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2012, primarily due to the installation of large production print and inserting equipment in North America and licensing revenue from providing our Volly™ software solution to Australia Post.

EBIT for the quarter and year-to-date periods increased significantly to \$14 million and \$17 million, respectively, compared to \$6 million and \$8 million in the prior year quarter and year-to-date periods, respectively, due to the increase in revenue and cost-reduction and productivity improvement initiatives.

#### Software

Revenue for the Software segment decreased 8% to \$92 million and 14% to \$173 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2012, primarily due to fewer large dollar licensing contracts in North America, and uncertain economic conditions and constrained public sector spending in our international markets. Software revenue in the prior year-to-date period also included \$13 million from two significant software contracts.

EBIT increased 85% to \$16 million in the quarter and 8% to \$21 million for the year-to-date period, compared to the same periods in 2012, primarily due to cost-reduction and productivity improvement initiatives.

#### Management Services



Revenue for the Management Services segment decreased 3% in both the quarter and year-to-date periods to \$175 million and \$351 million, respectively, compared to the same periods in 2012, primarily due to lost business and continued pricing pressure on new business and contract renewals. Despite the reduction in revenue, EBIT increased 4% to \$15 million in the quarter and 11% to \$29 million in the year-to-date period, compared to the same periods in 2012, due to lower operating costs and productivity improvements.

#### Mail Services

Revenue for the Mail Services segment increased 10% to \$119 million and 7% to \$238 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2012, primarily due to revenue from our ecommerce cross-border package delivery solution and growth in presort volumes for both Standard mail and First Class mail.

EBIT for the quarter decreased 46% to \$15 million and 44% to \$35 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2012. The decrease in EBIT was primarily due to continuing investment in the growth of our ecommerce offering and margin compression. EBIT for the prior year quarter and year-to-date periods also included benefits from fire-related insurance recoveries of \$4 million and \$11 million, respectively.

#### Marketing Services

Revenue for the Marketing Services segment decreased 17% to \$30 million and 16% to \$55 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2012, and EBIT decreased 44% to \$4 million and 50% to \$6 million in the quarter and year-to-date periods, respectively, compared to the same periods in 2012. The decrease in revenue and EBIT was due to lower marketing fees under certain contract renewals. We expect that similar revenue and EBIT trends will continue throughout the year.

#### LIQUIDITY AND CAPITAL RESOURCES

We believe that cash generated from operations, existing cash and investments, borrowing capacity under our commercial paper program and our credit facility are currently sufficient to support our cash needs, including business operations, debt repayments, customer deposits and discretionary uses such as capital investments, dividends and share repurchases. Cash and cash equivalents and short-term investments were \$631 million at June 30, 2013 and \$950 million at December 31, 2012.

We have had the ability to supplement short-term liquidity through our consistent and uninterrupted access to the commercial paper market to date. We have an effective shelf registration statement and the ability to fund the long-term needs of our business through broad and efficient access to capital markets, cash flow, proceeds from divestitures and a credit facility.

Within the last 12 months, the rating agencies reduced our credit ratings. There can be no assurances that one or more of the rating agencies will not take additional adverse actions in the future.

We continuously review our liquidity profile through published credit ratings and the credit default swap market. We also monitor the creditworthiness of those banks acting as derivative counterparties, depository banks or credit providers.

#### Cash Flow Summary

Net cash provided by operating activities for the six months ended June 30, 2013 was \$279 million compared to \$340 million for the six months ended June 30, 2012. The decrease in cash flow from operations is due to the cash payment of \$27 million for the call premium and transaction fees in connection with the Tender Offer (see below), higher payments of accounts payable and accrued liabilities and higher income tax payments. Cash flow from operations in the current year benefited from a special contribution of \$95 million to our pension plans in 2012, lower inventory purchases of \$39 million, lower restructuring payments of \$21 million and proceeds of \$5 million from the unwinding of interest rate swaps.

Net cash used in investing activities for the six months ended June 30, 2013 was \$86 million, compared to cash provided by investing activities of \$15 million for the six months ended June 30, 2012. Cash flow from investing activities in 2012 included proceeds of \$106 million received from the sale of leveraged lease assets.

Net cash used in financing activities for the six months ended June 30, 2013 was \$487 million compared to \$705 million for the six months ended June 30, 2012. See Financings and Capitalization section below for details of significant cash flows from financing activities.

#### Financings and Capitalization

We are a Well-Known Seasoned Issuer as defined in the Securities Act, which allows us to issue debt securities, preferred stock, preference stock, common stock, purchase contracts, depository shares, warrants and units in an expedited fashion. We have a commercial paper program that is an important source of liquidity for us and a

committed credit facility of \$1.0 billion to support our commercial paper issuances. The credit facility expires in April 2016. We have not drawn upon the credit facility.

As of June 30, 2013, there were no outstanding commercial paper borrowings. During the quarter, commercial paper borrowings averaged \$75 million at a weighted-average interest rate of 0.46% and the maximum amount outstanding at any time was \$100 million.

During the year, we completed a cash tender offer (the Tender Offer) for a portion of our 4.875% Notes due 2014, our 5.0% Notes due 2015, and our 4.75% Notes due 2016 (the Subject Notes). Holders who validly tendered their notes received the principal amount of the notes tendered, all accrued and unpaid interest and a premium amount. An aggregate \$405 million of the Subject Notes were tendered and a net loss of \$25 million was recognized, consisting of the cash payment for the call premium and transaction fees and write-off of unamortized costs, partially offset by a net gain from the unwinding of interest rate swap agreements.

In March 2013, we issued \$425 million of 6.7% fixed-rate 30-year notes (net proceeds received after fees and discount were \$412 million). Interest is payable quarterly. The notes mature in 2043, but may be redeemed, at our option, in whole or in part, at any time on or after March 7, 2018 at a redemption price equal to 100% of the principal amount, plus accrued and unpaid interest. The net proceeds were used to fund the Tender Offer.

In June 2013, the \$375 million 3.875% notes matured and were redeemed with cash.

Cash and cash equivalents held by our foreign subsidiaries are generally used to support the liquidity needs of these subsidiaries. Most of these amounts could be repatriated to the U.S. but would be subject to additional taxes.

Repatriation of some foreign balances is restricted by local laws. Cash and cash equivalents held by our foreign subsidiaries were \$297 million at June 30, 2013 and \$219 million at December 31, 2012.

We paid dividends to our common stockholders in the amount of \$113 million (\$0.5625 per share) for the six months ended June 30, 2013 and \$150 million (\$0.75 per share) for the six months ended June 30, 2012. Each quarter, our Board of Directors considers our recent and projected earnings and other capital needs and priorities in deciding whether to approve the amount and payment of a dividend. On July 30, 2013, our Board of Directors declared a cash dividend of \$0.1875 per share, payable on September 12, 2013. There are no material restrictions on our ability to declare dividends.

#### Regulatory Matters

There have been no significant changes to the regulatory matters disclosed in our 2012 Annual Report.

#### Item 3: Quantitative and Qualitative Disclosures about Market Risk

There were no material changes to the disclosures made in the 2012 Annual Report regarding this matter.

#### Item 4: Controls and Procedures

Disclosure controls and procedures are designed to reasonably assure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures are also designed to reasonably assure that such information is accumulated and communicated to our management, including our Chief Executive Officer (CEO) and Chief Financial Officer (CFO), as appropriate to allow timely decisions regarding required disclosure.

Under the direction of our CEO and CFO, we evaluated our disclosure controls and procedures (as defined in Rule 13a-15(e) and Rule 15d-15(e) under the Exchange Act) and internal control over financial reporting. Our CEO and CFO concluded that, as of the end of the period covered by this report, such disclosure controls and procedures were effective to ensure that information we are required to disclose in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Exchange Act. In addition, no changes in internal control over financial reporting occurred during the fiscal quarter covered by this report that have materially affected, or are reasonably likely to materially affect, such internal control over financial reporting. It should be noted that any system of controls is based in part upon certain assumptions designed to obtain reasonable (and not absolute) assurance as to its effectiveness, and there can be no assurance that any design will succeed in achieving its stated goals. Notwithstanding this caution, the disclosure controls and procedures are designed to provide reasonable assurance of achieving their stated objectives, and the CEO and CFO have concluded that the disclosure controls and procedures are effective at that reasonable assurance level.

## PART II. OTHER INFORMATION

### Item 1: Legal Proceedings

See Note 14 to the unaudited Condensed Consolidated Financial Statements.

### Item 1A: Risk Factors

There were no material changes to the risk factors identified in the 2012 Annual Report.

### Item 2: Unregistered Sales of Equity Securities and Use of Proceeds

#### Repurchases of Equity Securities

We periodically repurchase shares of our common stock to manage the dilution created by shares issued under employee stock plans and for other purposes in the open market. As of June 30, 2013, we have remaining authorization to repurchase up to \$50 million of our common stock. There were no share repurchases during the quarter ended June 30, 2013.

### Item 6: Exhibits

| Exhibit Number | Description  |
|----------------|--|
| 12             | Computation of ratio of earnings to fixed charges  |
| 31.1           | Certification of Chief Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as amended |
| 31.2           | Certification of Chief Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as amended |
| 32.1           | Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350  |
| 32.2           | Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350  |
| 101.INS        | XBRL Report Instance Document  |
| 101.SCH        | XBRL Taxonomy Extension Schema Document  |
| 101.CAL        | XBRL Taxonomy Calculation Linkbase Document  |
| 101.DEF        | XBRL Taxonomy Definition Linkbase Document   |
| 101.LAB        | XBRL Taxonomy Label Linkbase Document  |
| 101.PRE        | XBRL Taxonomy Presentation Linkbase Document   |

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

PITNEY BOWES INC.

Date: August 1, 2013

/s/ Michael Monahan

Michael Monahan  
Executive Vice President and Chief Financial Officer  
(Principal Financial Officer)

/s/ Steven J. Green

Steven J. Green  
Vice President – Finance and Chief Accounting Officer  
(Principal Accounting Officer)

Exhibit Index

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| 101.PRE        | XBRL Taxonomy Presentation Linkbase Document   |